Small Business Working Committee

report to ministers

BREAKING THROUGH BARRIERS

FORGING OUR FUTURE

Copies of the report are available from:

Publications Centre
Industry Canada
Second Floor, East Tower
235 Queen Street
OTTAWA, Ont.
K1A 0H5

Tel.: (613) 954-5716
Fax: (613) 954-6436

Acknowledgment

Financial support from the Government of Canada to pay for the publication of this report is gratefully acknowledged.

The views expressed in this report are not necessarily those of the Government of Canada.

Cat. No. C2-253/1994E
ISBN 0-662-22794-8
SISB PU 0035-94-01

Aussi disponible en français sous le titre *Franchir les obstacles : Bâtir notre avenir.*

SMALL BUSINESS
WORKING COMMITTEE

Report to Ministers

BREAKING THROUGH BARRIERS

FORGING OUR FUTURE

Government of Canada Gouvernement du Canada

Canada

Table of Contents

MEMBERS OF THE SMALL BUSINESS WORKING COMMITTEE

The following individuals have participated in the Small Business Working Committee over the last six months. The positions taken in this report represent the majority opinion of the group involved. Not every recommendation has been agreed to by every individual on the committee, or the organizations they represent. November 14, 1994.

Brien G. Gray, Co-chair
Small Business Working Committee
Senior Vice-President, Policy and Research
Canadian Federation of Independent Business

Phil O'Brien, Co-chair
Small Business Working Committee
Past Chairman, Canadian Chamber of Commerce
Chairman & CEO, Devencore Ltd.

Nancy Adamo
President
Hockley Valley Resort Ltd.

Carolyn Armstrong
Vice President
Toronto Bio-technology Initiative

Mona Bandeen
Chair
Canadian Women Entrepreneur of the Year Awards

Claire Boulanger
Vice-présidente
Services de Restaurant PHM inc.

Bev Brennan
Vice President, Finance
Philom Bios

Jeff Burnham
President
Working World Training Centre

Geoff Cannon
Executive Director
Institute for Small Business
Bank of Montreal

Tom Cumming
President and CEO
The Alberta Stock Exchange

Don Eastcott
President
Eadon Companies Group
Managing Director and Corporate Secretary
Canadian Organization of Small Business Inc.

Shirley-Ann George
Executive Director, Ottawa
Canadian Advanced Technology Association

John Gow
President
Silver Star Mountain Resort

Frank Heaps
President
The Upper Canada Brewing Company

Gilles Labbé
Chairman and CEO
Héroux Inc.

Yvon Lafortune
Président et CEO
Nova Bus Corporation – Corporation
Nova Quintech

Larry Licharson
President
Corporate Media Services Ltd.

Dennis Mills, M.P.
Broadview-Greenwood
Parliamentary Secretary
to the Minister of Industry

Jim Moore
Vice President, Policy
Canadian Exporters Association

Barbara Mowat
President
Impact Communications Ltd.

Janice Moyer
President & CEO
Information Technology Association of Canada

Jayson Myers
Chief Economist
Canadian Manufacturers' Association

Pierre Reid
Recteur
Université de Sherbrooke

Paul Richards
President
Proscience Inc.

Aubrey Rogers
Treasurer
Cape Breton Bulk Carriers

Cathy Rose
President
Creative Esthetics Dental Lab Inc.

Stuart Smith
President
Philip Utilities Management Corporation

Garth Steele, C.A.
GST Partner
Welch and Company

David Walker, M.P.
Winnipeg North Centre
Parliamentary Secretary
to the Minister of Finance

Dennis Wood
Chairman & CEO
C-MAC Industries

Warren Walker
Senior Vice President
Bank of Nova Scotia

Larry Zepf
President
Zepf Technologies

Rod White
Vice President
NewEast Technologies Inc.

Preface

In the February 1994 budget document *Growing Small Businesses*, the Minister of Finance, The Honourable Paul Martin and the Minister of Industry, The Honourable John Manley, invited representatives from the private sector to provide the government with practical recommendations addressing a variety of issues currently confronting the small- and medium-sized business sector. In May 1994, the Small Business Working Committee, originally comprised of two groups, the Business Environment Committee and the Committee on Growth Issues, met for the first time.

Following their first meeting, and in order to address the variety of issues confronting them, they formed six subgroups to address the issues of: taxation, financing, regulation and paper burden; skills development; science and technology; and international trade.

The Committee has met some 16 times throughout the spring, summer and fall, and have received presentations from a broad range of public and private sector representatives on a variety of small business issues.

The Committee was supported in its activities by a Secretariat comprised of the following individuals:

Michael Flaherty, Nathalie Lavallée — Industry Canada

Gerry Birks — Department of Finance

Marcel Plamondon — Federal Office of Regional Development (Québec)

Ken Littlepage — Atlantic Canada Opportunities Agency

Christine Winiarz-Searle — Western Economic Diversification Canada

Minh Trinh — Human Resources Development Canada

Pamela Richmire — Department of Justice.

In addition, the Committee wishes to thank the many other individuals who donated their time to ensure the work was done.

Executive Summary

A world of unrelenting change presents unlimited opportunities. Those willing to take advantage of these opportunities need to be innovative and courageous. They need to rise above the ordinary and challenge the status quo.

Canadian entrepreneurs have demonstrated their ability to be innovative and dynamic. The small businesses they own and operate represent channels for the energy and creativity of an increasing number of individual Canadians. Small businesses exist in every corner of this country, from large metropolitan areas to tiny and remote communities. To ignore this vast pool of entrepreneurial energy is to miss a tremendous opportunity for the Canadian economy.

THE SMALL BUSINESS WORKING COMMITTEE

Through the February 1994 budget, The Honourable John Manley, Minister of Industry, and The Honourable Paul Martin, Minister of Finance, extended an invitation to bring together representatives of Canada's small and medium enterprise (SME) community to advise on what action should be taken to ensure continued SME growth. The specific mandate of the Committee was:

- to provide advice on the real problems faced by SMEs and the types of assistance that they really need; and
- to recommend new approaches to ensure sustainable SME growth.

The Committee consisted of a wide range of representatives and stakeholders drawn from the SME community across Canada.

WHY IS SMALL BUSINESS SO SIGNIFICANT?

Small business has come of age in Canada. Over the past two decades, the number of new businesses in Canada has surged. Significantly, 99 percent of this country's small businesses employ fewer than 100 people. An additional 1.5 million individuals are currently self-employed.

Taken together, the small business sector now accounts for approximately 40 percent of Canada's GDP. It is responsible for more than a quarter of all sales, a third of all profits and a fifth of all assets. Even more striking, the small business sector now accounts for over half of all private sector employment. Clearly, the impact of small business on the Canadian economy is profound and will continue to be relied upon for economic growth and job creation.

WHAT BARRIERS DOES SMALL BUSINESS FACE?

As we enter the 21st century, Canada's SMEs confront significant challenges.

- Public policies of the past three decades have left Canada with a massive federal debt, an alarming deficit, high taxes and a rigid regulatory environment. These are onerous barriers that seriously impact small business growth.
- Assessing suitable financial support is critical to the expansion of SMEs. Without adequate financing, the growth of these businesses will be stunted and our future prosperity threatened.
- Technology has given small firms the tools to extend their reach and increase productivity. Technology has also intensified competition; small businesses must remain technologically competitive if they are to survive and grow.
- Owners and employees in today's business environment require new and more sophisticated skills.

- The global economy has had a profound impact on our domestic economy — we now must compete directly with the best in the world.

We need to address the significant barriers that stand in the way of unleashing the entrepreneurial potential within our SMEs — primarily government debt, taxes and regulation.

Government debt is fast approaching the unsupportable. Over the long term, debt reduction can only be achieved if government expenditure cuts are accompanied by policies which allow SMEs the freedom to create wealth and jobs. Governments must also manage their affairs better. They need to reduce and re-orient programs not only to cut costs, but to improve the way they interact with small businesses.

Taxes, at all levels, are too high. The effective tax burden on small business has continuously increased primarily because of increases to profit-insensitive taxes (e.g., UI premiums, Canada Pension Plan, Worker's Compensation and property taxes).

Our regulatory system costs businesses time and money — existing regulatory requirements create inefficiencies, reduce flexibility and impede innovation.

THE PRIORITIES FOR CHANGE

Small businesses are highly entrepreneurial and opportunity-driven. Governments must provide an environment in which they will be motivated to remain and grow in Canada. Given this reality, the Committee has identified the most urgent priorities for Canadian SMEs and presented recommendations designed to address them. To show how these recommendations can be achieved, the Committee has provided detailed implementation plans for each recommendation.

Together, these recommendations constitute a package of practical, common-sense initiatives that, if implemented, will improve the competitive position of small business and provide a sound basis for its further growth and development.

- **Cut profit-insensitive taxes**: There has been an increased reliance on profit-insensitive taxes by all levels of government. These levies are primarily payroll taxes but also include business and licensing fees, and property taxes. Together, these levies amount to a tax on job creation and a depletion of equity capital. For small businesses, they result in lower retention of profits and greater reliance on external financing. The Committee recommends that the federal government reduce the burden of its own profit-insensitive taxes (specifically UI and CPP) and partner with the provinces and municipalities to ensure they jointly redress this fundamental impediment in the system.
- **Boost equity financing**: Equity financing is a fundamental need for small business. Small businesses have difficulty raising equity capital primarily because of the relatively small amounts of equity that they require compared to the costs and risks facing potential investors. The Committee recommends that the federal government support the provision of equity financing for small businesses by providing new tax incentives for private investors, ensuring that current incentives such as the Labour-Sponsored Venture Capital Corporation are effective and supporting the establishment of community-based equity financing programs.
- **Increase financial institution participation in debt financing**: Small businesses find it difficult to obtain debt financing from traditional financial institutions. Such institutions claim they are unable to service small loans economically. They use conventional risk assessment policies which do not favour small business, and they do not face the kind of competition that would encourage them to pay attention to this market. The Committee recommends that the major financial institutions increase their participation in small business financing, and that the federal government use its leverage to increase competition among these institutions to ensure that they significantly increase their appetite for lending in this market.

- **Increase Small Business Deduction**: Small businesses have access to the Small Business Deduction (SBD) which reduces the federal tax rate on active business income below $200 000. The $200 000 threshold, set in 1982, has not been indexed to inflation, nor has it reflected significant recent increases in profit-insensitive taxes. The Committee recommends that the federal government adopt graduated SBD tax rates and increase the threshold to $400 000, thereby encouraging the continued growth of businesses that are currently just over the $200 000 threshold by enabling more internal financing.
- **Stimulate SME exporting**: A critical step in the exporting process occurs at the detailed market research stage when a business has to make a serious commitment backed by time, effort and money. Small businesses can be encouraged to make this commitment if they feel that some of their investment in market research can be recovered. To accomplish this, the Committee recommends that the federal government implement a refundable tax credit against foreign market research and development expenditures.
- **Reduce tax complexity and compliance costs**: The complexity of tax administration and onerous compliance costs at both the federal and provincial levels impose a disproportionate burden on small businesses which usually have limited resources and limited internal expertise. The Committee recommends that all levels of government reduce complexity and compliance costs by simplifying and harmonizing the tax system and adopting the goals of efficiency, consistency, cooperation and fairness in their dealings with small business.
- **Refocus government financing programs**: Government programs to support debt financing for small business have proliferated with the result that there is now substantial overlap in program activities and duplication of administrative bureaucracies. This has increased the cost of delivering government assistance and served to discourage SMEs from using the system because of its complexity. The Committee recommends that the federal government significantly reduce its own debt levels which will serve to lower the cost and increase the availability of funds for small business. This can be achieved by reducing and rationalizing government programs. Remaining government-sponsored programs should be refocused to fill financing gaps not currently served by the private sector.
- **Scientific Research and Experimental Development (SR&ED) Tax Credit**: Canadian sources of financing for knowledge-intensive ventures remain scarce. The refundable portion of the SR&ED tax credit allows firms to maintain the cash flow needed to fund innovative projects. The Committee recommends that the current federal investment tax credit must be maintained and expanded to include a broader scope of innovation activities.
- **Reduce and rationalize regulations**: Too many regulations are developed and administered with little consideration given to their impact on the competitiveness of small businesses. Government must regulate less, simplify paperwork, limit information requirements and get out of the way so that small business can focus on creating wealth and jobs. Reducing regulatory burden will save the government money and will yield tremendous benefits in terms of small business productivity and competitiveness. The Committee recommends that the federal government remove unnecessary, ineffective or uncompetitive regulations, rationalize existing regulations across departments and encourage regulatory flexibility.

FISCAL NEUTRALITY

Some of the recommendations made by the Committee will save money, some are fiscally neutral and some represent additional spending in the form of foregone tax revenues. To offset any additional costs to the government, the Committee is in favour of a comprehensive review of current small business programs which, it believes, will result in substantial savings through the elimination of many programs and the refocusing of others.

Where the Committee has recommended incentives, it does so on the understanding that they be paid for from savings realized through the rationalization and reduction of existing programs. The Committee believes that providing appropriate support and incentives to small business will yield more wealth creation which will, in turn, sustain employment, foster growth and generate additional tax revenues.

URGENT NEED FOR ACTION

A unique opportunity exists to harness the entrepreneurial energy of Canadian SMEs. Grasping this opportunity will enable Canada to compete and prosper in the emerging and very competitive world economy. However, the barriers imposed on small business by all levels of government must be recognized and reduced. If this is not the case and the barriers keep proliferating, small businesses will be unable to do the one thing that they are best capable of doing — creating the wealth that is the key to meeting our national fiscal and employment goals.

The real issue now comes down to what governments are prepared to do to abandon outdated approaches and initiate significant changes in small business policy. When Finance Minister Paul Martin and Industry Minister John Manley asked the members of the Small Business Working Committee for their advice, they emphasized that they were looking for concrete recommendations by the fall of 1994. The Committee believes that it has done what was asked. It is now up to the federal government to respond by acting promptly and decisively.

Though the formal work of the Committee is over, its members, along with the entire small business community, will be watching what happens with keen interest. The present administration has an opportunity to restore the federal government's credibility with small business. The Committee sincerely hopes that it takes advantage of this opportunity.

Copies of the report are available from:

Publications Centre
Industry Canada
Second Floor, East Tower
235 Queen Street
OTTAWA, Ont.
K1A 0H5
Tel.: (613) 954-5716
Fax: (613) 954-6436

Introduction

1

A world of unrelenting change presents unlimited opportunities. Those willing to take advantage of these opportunities need to be innovative and courageous. They need to rise above the ordinary and challenge the status quo.

Canadian entrepreneurs have demonstrated their ability to be innovative and dynamic. The small businesses they own and operate represent channels for the energy and creativity of an increasing number of individual Canadians. Small businesses exist in every corner of this country, from large metropolitan areas to tiny and remote communities. To ignore this vast pool of entrepreneurial energy is to miss a tremendous opportunity for the Canadian economy.

THE SMALL BUSINESS WORKING COMMITTEE

Through the February 1994 budget, The Honourable John Manley, Minister of Industry, and The Honourable Paul Martin, Minister of Finance, extended an invitation to bring together representatives of Canada's small and medium enterprise (SME) community to advise on what action should be taken to ensure continued SME growth. The specific mandate of the Committee was:

- to provide advice on the real problems faced by SMEs and the types of assistance that they really need; and
- to recommend new approaches to ensure sustainable SME growth.

The Committee consisted of a wide range of representatives and stakeholders drawn from the SME community across Canada.

WHY IS SMALL BUSINESS SO SIGNIFICANT?

Small business has come of age in Canada. Over the past two decades, the number of new businesses in Canada has surged. Significantly, 99 percent of this country's small businesses employ fewer than 100 people. An additional 1.5 million individuals are currently self-employed.

Taken together, the small business sector now accounts for approximately 40 percent of Canada's GDP. It is responsible for more than a quarter of all sales, a third of all profits and a fifth of all assets. Even more striking, the small business sector now accounts for over half of all private sector employment. Clearly, the impact of small business on the Canadian economy is profound and will continue to be relied upon for economic growth and job creation.

WHAT IS A SMALL BUSINESS?

There are many ways of defining a small or medium business. Perhaps the most common definition relates to the number of jobs it supports. In Canada, small businesses are generally considered to be enterprises with fewer than 100 employees in the manufacturing sector and fewer than 50 in services, while medium businesses employ up to 500 people. Another definition measures wealth creation: small businesses are those that have annual sales below $5 million, while medium businesses sell up to $50 million annually. Another way of thinking about business size is in relation to other enterprises in the same sector. In some industries dominated by very large firms or in international markets, a business employing hundreds of workers may still be considered quite small.

As we enter the 21st century, Canada's SMEs confront significant challenges.

- Public policies of the past three decades have left Canada with a massive federal debt, an alarming deficit, high taxes and a rigid regulatory environment. These are onerous barriers that seriously impact small business growth.
- Accessing suitable financial support is critical to the expansion of SMEs. Without adequate financing, the growth of these businesses will be stunted and our future prosperity threatened.
- Technology has given small firms the tools to extend their reach and increase productivity. Technology has also intensified competition; small businesses must remain technologically competitive if they are to survive and grow.
- Owners and employees in today's business environment require new and more sophisticated skills.
- The global economy has had a profound impact on our domestic economy — we now must compete directly with the best in the world to survive.

SMALL BUSINESS — OUR BEST OPPORTUNITY

As governments and large corporations downsize and outsource activities, a growing number of Canadians will either create their own jobs or work for small businesses. Moreover, the emergence of a new, knowledge-intensive economy supported by sophisticated information technologies will allow many more Canadians to become entrepreneurs. In the future, most Canadians will spend their working lives in small businesses.

Governments can best help Canadians make this transition by making it easier for them to create, maintain and expand their own businesses. They should focus their efforts on creating a favourable business environment by reducing taxes, eliminating deficits and rationalizing their own activities. In this way, small business will benefit from a nurturing environment that can support growth and encourage international competitiveness, and provide unemployed Canadians with the hope that improved job opportunities will afford.

WHY DO SMALL BUSINESSES EXIST?

It is crucial for policy-makers to understand that small businesses do not exist to grow and they do not exist to create jobs — they exist to create wealth for their owners and shareholders. They will only grow and they will only hire people if by doing so they create additional wealth for those owners and shareholders. As a result, owners and shareholders must concentrate on what should be their real focus — efficiency, productivity and competitiveness in the interests of long-term profitability.

Small business is often thought of as a single economic force. In fact, small business represents a diversity of business types, interests and concerns. Small business can be differentiated on the basis of numerous characteristics: size, stage of life cycle, growth rates, ownership, sector, geographic location and strategic focus, to name a few. What is common to all these types of businesses, however, is an entrepreneurial desire to make their own decisions, to achieve their best, to contribute to their communities and to see their efforts rewarded.

Ultimately, if the real purpose of a small business is wealth creation, then the best way governments can support small business is to adopt measures that will help it achieve that purpose. That will, in the first instance, means allowing small businesses to retain more of the wealth that they create to invest in future growth. It will also mean implementing measures and incentives that help small business move into wealth-creating activities, such as enhancing domestic competitiveness, pursuing technological innovation and international market development.

FUNDAMENTAL PRINCIPLES FOR GOVERNMENT

There are a number of fundamental principles that governments should adopt in future policy-making aimed at growing small business. As priorities, governments should:

- remove themselves from the market and let it function freely rather than seek to influence or distort it;
- restrict their own activities to filling gaps not currently served by the private sector and they should do so only on a temporary basis until the private sector can take over;
- redesign the taxation system as a vehicle for economic development rather than its current narrow role as a generator of tax revenues;
- focus on helping small businesses access the information and intelligence they require.

Business has had to redefine and re-engineer itself in the marketplace in order to survive. Government must do the same. And it must do so using many of the same tools: client-oriented service improvements, a focus on the bottom line, strict accountability, measuring results and emphasizing effectiveness.

In implementing these principles, governments should employ the following operational methods:

- use business-like principles of management;
- design and test all initiatives with end-users;
- measure effectiveness and return on investment, not just activity;
- strengthen partnering between departments, among different levels of government, and between government and non-government organizations; and
- avoid turf wars or jurisdictional disputes between departments and levels of government.

THE BURDEN OF GOVERNMENT

There are two principal burdens imposed on small business by government that have increased substantially over the past two decades and which are now limiting the ability of small business to make its full contribution to the growth and stability of the Canadian economy.

The Tax and Debt Burden

High taxes are the inevitable consequence of high deficits and growing debt. For more than two decades, Canadians have allowed governments to act as if there were no limits to what they could do, and spend as if there were no tomorrow. However, tomorrow has become today and all Canadians are now liable for paying the bills.

To escape from the debt trap, governments are casting about for additional sources of revenues and have fastened, in part, upon small business. The burden of taxation levied on small business has increased substantially over this period. In addition, the sheer complexity and inefficiency of the tax system has resulted in countless hours of costly paperwork. It must be realized that business is not an inexhaustible source of taxable wealth. The more it is taxed, the less capital it will have to invest in future wealth creation.

An alternative way of reducing deficits and debt at all levels of government is through reduction in the number and cost of government business programs. These program changes should be based on an assessment of their effectiveness and efficiency.

The Regulatory Burden

Taxation and the deficit weigh heavily on small business, but that weight is compounded by the additional burdens imposed by regulatory intervention and interference of government in the operations of business. The bottom line for business is cost. Government regulatory burden costs business time and money. It costs businesses in terms of competitiveness when regulatory information requirements create inefficiencies, reduce flexibility and impede innovation. The unproductive time spent complying with government demands represents a massive opportunity cost to Canadian business and the Canadian economy.

URGENT NEED FOR ACTION

A unique opportunity exists to harness the entrepreneurial energy of Canadian SMEs. Grasping this opportunity will enable Canada to compete and prosper in the emerging and very competitive world economy. However, the barriers imposed on small business by all levels of government must be recognized and reduced. If this is not the case and the barriers keep proliferating, small businesses will be unable to do the one thing that they are best capable of doing — creating the wealth that is the key to meeting our national fiscal and employment goals.

The real issue now comes down to what governments are prepared to do to abandon outdated approaches and initiate significant changes in small business policy. When Finance Minister Paul Martin and Industry Minister John Manley asked the members of the Small Business Working Committee for their advice, they emphasized that they were looking for concrete recommendations by the fall of 1994.

The Committėe believes that it has done what was asked of it. It reviewed and analyzed a number of areas of activity in which small business and government interface with each other — taxation, financing, regulation, skills development, science and technology, and international trade development. Based on this analysis, the Committee has prepared this report on how this interface can be made more effective and efficient as well as less costly to both government and small business. It is now up to the federal government to respond by acting promptly and decisively.

Taxation

THE OPPORTUNITY

The most fundamental way in which all small businesses interact with government is through the tax system. Governments must reform their tax systems to facilitate the creation of wealth by small business. It is through the increased wealth of small business that governments will realize an increase in tax revenue, thereby helping governments reduce their debt.

Canada's tax systems (federal, provincial and municipal) have imposed a disproportionate burden on small business. This burden has impaired the competitiveness of small- and medium-sized enterprises (SMEs) and their ability to create wealth and therefore jobs. One of the most significant factors contributing to this higher tax burden has been the increased use of profit-insensitive taxes on the part of all levels of government.

Taxes that are not based on profits represent approximately 70 percent of all direct taxes paid by corporations.

Department of Finance

The growing complexity of the tax system has resulted in disproportionate compliance costs for small business. In addition, the benefits provided by the Small Business Deduction (SBD) have been eroded by inflation. As a result, small business is limited in its ability to retain earnings and maintain equity for continued growth. In order to grow, small business is forced to rely on external sources of financing, which are extremely difficult to find and access.

Public policies which emphasize increased taxes on SMEs act as a deterrent to growth. The tax system should not be used exclusively as a tool for raising revenue. The Committee is concerned that using the tax system as the primary tool to address the deficit will not solve our fiscal and economic problems. The government has an opportunity to shift the emphasis toward using tax policy to encourage and support SME growth. Effectively, the less SMEs are taxed, the more capital will be available to invest in future growth and job creation.

First Principles of Small Business Taxation

- Tax systems at all levels must support the creation and growth of viable small businesses.
- Tax measures should not result in disincentives to hire.
- Canada's tax systems must reduce their dependence on all forms of profit-insensitive taxes.
- Tax systems must be simplified to reduce the compliance costs borne by small business and free up productive capacity.
- Tax systems must encourage the retention of profits to finance the internal growth of small businesses.
- The federal, provincial and municipal governments must coordinate and simplify their tax systems to ensure that the total tax burden on small businesses is fair and reasonable.
- Potential reductions in tax revenues must be balanced by reductions in government spending.

PROFIT-INSENSITIVE TAXES

The growing reliance by all levels of governments on revenues from taxation that is not related to profit (profit-insensitive taxes) is an unacceptable trend. The Committee recognizes that increases in such taxes allow governments to secure a more stable tax base. However, this approach conflicts with the stated goals of all levels of government to create and maintain jobs.

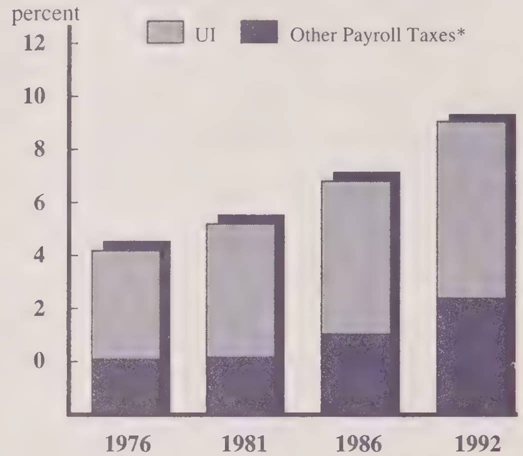
Profit-insensitive taxes include payroll taxes such as: premiums for Unemployment Insurance (UI), Canada/Quebec Pension Plan (CPP/QPP) and Workers' Compensation (WC). In some provinces, payroll taxes also include health insurance premiums (which can be as high as 3.75 percent in Quebec). Other onerous profit-insensitive taxes are business and licensing fees as well as municipal property taxes, which have grown from 23 percent of all corporate levies in 1986 to 27 percent in 1992.[1]

The single most disquieting feature of payroll levies is that they amount to a direct tax on job creation. Recent increases in these types of taxes and their high current levels impose a disproportionate burden on small businesses. The burden of payroll taxes tend to fall most heavily on labour-intensive businesses, or those operating at low or negative profit margins.

For small businesses facing increased pressures on profit margins, relatively high increases in profit-insensitive taxes imply lower retention of profits, higher vulnerability to recessionary times and increased reliance on external financing. In addition, payroll taxes are added to the cost of goods and services produced and are included in the price of exports, thereby reducing the international competitiveness of Canadian businesses.

The Committee's view reflects the overwhelming consensus within the business community in affirming that a reduction of these taxes would have a positive impact on hiring, job maintenance and wealth creation in the small business sector.

Payroll Taxes in Canada as a share of labour compensation



Source: Statistics Canada and Department of Finance

**Other Payroll Taxes include Workers' Compensation premiums, Canada and Quebec Pension Plan premiums, provincial employment and health taxes, and municipal business and property taxes.*

Despite the continued use of premium increases, many programs supported by these taxes and premiums are seriously underfunded. For example, according to the chief actuary of the CPP, the unfunded liability of the Plan has grown from $81 billion in 1977 to $491 billion in 1993. As a result, the CPP/QPP projected contribution rates are expected to increase from 5 percent to 8.90 percent by the year 2010.[2]

Premium rates tend to increase during the latter parts of a recession in order to even out deficits and surpluses in the UI account over a recessionary period. During a prolonged recession, this tax on jobs is increasing precisely at the time when jobs are most scarce and businesses are least able to bear the tax.

Human Resources Development Canada

Similarly, recent estimates show a cumulative deficit of $5.9 billion in the UI program as of 1993.[3] To finance UI, the insurance premium is now 3.07 percent for employees and 4.298 percent for employers — 140 percent of the employee rate.[4] Although recent statistics suggest some improvement in UI funding levels, underfunding will continue to exist in the foreseeable future and implies continued pressure on governments to increase these premiums further. As long as there are no long-term structural changes to the UI program beyond what the federal government has recently proposed, cyclical underfunding will continue.

Workers' Compensation Boards (WCBs) in many provinces have large unfunded liabilities, which may lead to further increases in WC premiums. In addition, the average benefit and assessable income levels under WC are rising in most provinces, and this results in pressure on premiums everywhere. This is further complicated by the fact that WC benefits are not taxable, even though contributions to WC are deductible. As a result, WCBs, which are established under provincial authority, set benefit levels on the assumption that benefits are not taxable (the benefit rate is generally 90 percent of after-tax earnings) to a xxx dollar maximum. There is concern that the non-taxation of WC benefits results in a high after-tax benefit rate and therefore a negative work incentive.[5]

The first responsibility of the [UI] governance structure must be the long-term financial health of the UI system. Both employers and employees need assurance that their premium dollars will be well spent from a long-term perspective.

Unemployment Insurance Reform Business Coalition

Many municipalities have found it easier to tax small businesses rather than residences, even though most of the revenue obtained goes to education rather than other services. Ironically, small businesses, by virtue of these high taxes, are then impeded from hiring the products of the education system they are forced to disproportionally support.

The trend toward increased reliance on profit-insensitive taxes will not be reversed until every level of government begins to look not only at its own need to raise revenues, but also at the cumulative impact of such taxes and the effect that these taxes have on reducing job creation. In the absence of a coordinated approach there will be no long-term solution. No level of government is willing to reduce its own share of these taxes unilaterally, because each level believes that such action would simply allow the other two levels to increase their own taxes.

There are no winners in this game. The competitiveness of small businesses is impaired while governments struggle to squeeze ever higher taxes from them. This vicious cycle can only be overcome through negotiation and cooperation between the federal and provincial governments as part of their current review of Canada's tax structure. The Committee strongly believes that the federal government must break out of the cycle through longer-term structural tax reform. The hope is that other governments, following the federal government's lead, will reverse the unfortunate trend and correct the inordinate burden on small business.

Recommendation

The federal government must reduce the burden of profit-insensitive taxes on small businesses, specifically by lowering premiums on Unemployment Insurance and Canada Pension Plan. Such reductions can be realized through restructured programs, improvements in the efficiency of program delivery and reductions in administrative costs.

The federal government must work with provincial governments to ensure that its leadership is followed at the provincial and municipal levels.

How to Get There

- Eliminate the funding of social, regional and economic objectives from the UI program. Under no circumstances should there be a special payroll tax for the purpose of financing general training. The beneficiaries of training activities from the UI program must be restricted to those individuals who have funded the program through the payment of premiums. Other benefits currently provided by the UI program which relate to broader economic or social programs should be funded from general tax revenues.
- Commit to achieving equality between employer and employee UI premiums within four years and to ongoing reductions of future premiums.
- Reduce the benefit and administrative costs of UI by reforming the overall structure of benefits and improving the efficiency and effectiveness of delivery.
- Review the CPP/QPP benefits (coverage, entitlements, etc.) and program administration to determine cost savings.
- Work with provincial governments to initiate a review of the WC benefits provided to all workers, their costs and the appropriate means of paying for them.
- Reduce program administration costs and premiums under the various provincial plans and replace other payroll taxes, such as health care taxes, with direct premiums or consumption taxes.
- Encourage provincial governments to press municipal governments, where appropriate, to reduce business and property taxes and licensing fees.
- Ensure that all profit-insensitive taxes remain deductible for income tax purposes.

TAX COMPLEXITY AND COMPLIANCE

The complexity of tax administration and compliance at both the federal and provincial levels imposes an unnecessary burden on SMEs because of their small size and lack of internal expertise. Canada's tax system seems to be more concerned with strict efficiency than with overall effectiveness. By emphasizing the design of rigid systems focused on the purity of compliance, tax administration can have the undesired effect of inhibiting wealth-creating activity. As a result, Canadian businesses contend with tax systems that are complex and costly to administer by both business and government.

Small business has a number of concerns associated with the complexity and compliance procedures of the tax system:

Harmonization

The conflict between the federal and provincial tax systems and among different provincial systems imposes unnecessary burdens on small business.

Coordination and Simplification

A lack of coordination and cooperation between branches of Revenue Canada has resulted in the delivery of contradictory tax information to small business. It has also led to needless complexity and duplication of services. Small business is especially concerned about:

- the separate remittances and reporting requirements of payroll deductions, goods and services tax, excise taxes and income tax instalments;

- lack of coordination in audits and collections;
- the gross extent of the information collected;
- shortcomings in the efficiency and quality of Revenue Canada's service; and
- the complexity of calculating taxable income and taxable benefits (e.g. automobile benefits, arbitrary or unrealistic deduction levels for legitimate meals and entertainment).

Penalties and Dispute Handling

Government has permitted the use of estimates in making remittances but it has also strengthened penalties for late remittances. As a result, small businesses are often penalized for honest errors in remitting. Although the Fairness Legislation was established to deal with unfair or inaccurate administration of penalties, the reality is that few small businesses are willing to risk reprisals by complaining about the treatment they receive. It is difficult for a small business to obtain a waiver of a penalty — the process is too formalized and costly. Small business taxpayers must be confident that their complaints are being looked at impartially by people who are not their accusers.

Clarity and Consistency

Advance rulings, interpretations of Taxation and Customs regulations and policy bulletins are difficult to understand and often issued on an untimely and inconsistent basis. Taxpayers regularly receive differing advice from various front-line Revenue Canada offices across the country. Policy changes within the tax system happen too frequently and without due consideration of the administrative effect on small business. Also, the format of basic tax forms changes too frequently and inconsistently.

Service to Taxpayers

Many small businesses complain about the quality and consistency of the service they receive from Revenue Canada's staff. In addition, they are bombarded by a steady stream of incomprehensible or seemingly irrelevant information. It appears that Revenue Canada's concept of service to the client is not yet adhered to by all the department's staff. The Committee acknowledges that Revenue Canada has attempted to resolve many of these problems. The Committee supports this effort. Unless fundamental changes are undertaken to reform attitudes and the culture of tax administration, small business will continue to bear an inordinate cost of compliance.

The Committee acknowledges that many of the issues noted above may be a reflection of tax policies developed by the Department of Finance. However, the small business sector bears a disproportionate share of the burden of implementing tax policies. The implementation of complex tax policies and managing the compliance of multi-level government taxes must be balanced against the need of small business for harmonized and easily implementable tax systems.

Many of the specific issues relating to tax administration are dealt with in greater detail in the chapter on "The Burden of Government" in this report.

Recommendation

Governments must reduce the complexity and the compliance costs of the tax system through simplification and harmonization. In addition, Revenue Canada's goal in dealing with small business should be efficiency, consistency, cooperation and fairness.

GOODS AND SERVICES TAX

The Committee reviewed the federal government's progress with the reform of the goods and services tax (GST), and supports its initial proposal to implement a harmonized federal and provincial sales tax system that would result in lower sales tax rates across Canada. The Committee strongly opposes any

proposals for GST reform that would involve a major tax increase on the part of provincial governments and/or further fragmentation of the income tax regime.

The Committee recognizes that it is unlikely that the government will meet its original deadline of January 1, 1996, for replacing the GST, but it believes it is more important to get the new measures right. While the Committee strongly supports the concept of sales tax harmonization, it believes that the implementation of this concept must not result in an overall tax increase or additional compliance costs for small businesses. A reformed federal sales tax system that is harmonized with provincial sales tax systems must reduce the sales tax compliance burden for the typical small business.

There is a concern that the anticipated magnitude of changes to the sales tax may pose another series of transition requirements that will be both onerous and costly to the typical small business. Small businesses have spent an enormous amount of time and money to implement the current GST. The implementation of a harmonized sales tax must not result in additional transition costs to small businesses.

In addition to sales tax harmonization, other specific sales tax issues have been raised during the Committee's discussions.

- The broad range of exemptions and zero-rating provisions in the GST has led to confusion and complications for small business. This problem should be corrected by eliminating as many exempting and zero-rating provisions as possible. It is recognized, however, that there are and will continue to be certain exemptions mandated by law, agreement or government policy.
- Small business operators understand the need for a consumption tax and realize that they are the logical collectors of such a tax on behalf of the government. However, any improvements in the administrative systems arising from harmonization must be consistent with small business practices and realities.

Recommendation

The federal government must pursue sales tax harmonization. Harmonization must not result in an overall tax increase. Any transition to a new system must not impose increased costs on small businesses.

CORPORATE INCOME TAX

Small businesses have access to the SBD, which lowers the basic federal corporate tax rate on the first $200 000 of taxable income from 28 percent to 12 percent. This deduction is intended to compensate in part for the inherent structural biases faced by small businesses, including higher regulatory compliance costs, higher costs of capital, less competition for financial services, fewer economies of scale, less influence over selling prices and weaker buying power.

> **The small business deduction ... provides small corporations with more after-tax income for investment and expansion to recognize the special financing difficulties they face.**
>
> *Department of Finance*

The current maximum level of income eligible for this deduction was established in 1982 and, despite the substantial inflation experienced in Canada since that time, it remains at $200 000. In addition, the corporate tax structure has remained unchanged even while the level of profit-insensitive taxes for small businesses has increased significantly during recent years. As a result, the current corporate income tax structure for small businesses no longer supports small business growth to the extent that it once did, since smaller firms still pay higher effective tax rates when all taxes are considered. Larger businesses, with lower effective tax rates, have higher rates of post-tax profitability and hence a greater capacity to plough back earnings into various types of investments.

Because of inflation, the SBD needs to be increased to encourage the continued growth of businesses that are currently just over the $200 000 taxable income level threshold by allowing them to retain more of their earnings to finance expansion. The doubling of the SBD limit will remove a strong disincentive for growth.

Recommendation

The federal government should adopt graduated Small Business Deduction tax rates based on the level of taxable income. At the same time, it should increase the Small Business Deduction threshold to $400 000 to strengthen the equity base of SMEs and to increase growth and job creation in higher-growth SMEs with profits in the $200 000 to $400 000 range.

How to Get There

Immediately adopt a graduated tax rate for SMEs with taxable income between $200 000 and $400 000. More specifically, the federal government should adopt the following income tax regime for SMEs:

Taxable income range ($)	Current tax rate %	Proposed tax rate %
up to 200 000	12	12
200 000 to 300 000	28	17
300 000 to 400 000	28	22
over 400 000	28	28

The Committee recognizes that the proposed change will have a revenue impact, but this impact can be reduced by phasing out its availability for those businesses subject to the current Large Corporations Tax.[6] In addition, eligibility for this benefit should be restricted to SMEs that retain earnings for internal financing purposes.

LIFETIME CAPITAL GAINS EXEMPTION (LCGE)

Capital gains accruing from the disposition of qualifying small business corporation shares are eligible for the $500 000 Lifetime Capital Gains Exemption (LCGE) introduced in May 1985. This exemption is available to both entrepreneurs and outside equity investors who have held shares in SMEs for a minimum of two years.

In 1991, some 26 000 taxpayers claimed this exemption. Since 1988, the federal tax expenditure arising from this exemption has been estimated at $625 million per year.[7] However, it is commonly recognized that many taxpayers claiming this tax provision during the past few years have "crystallized" significant accrued gains on shares in their small business corporations, which continue to be controlled by the taxpayer after this process is concluded. In other words, the gains taxed under LCGE have not always resulted from the actual disposition of investments.

The Department of Finance is currently involved in a consultation process to seek inputs on the evaluation of the current system and possible replacement measures. In examining how well the LCGE has contributed to achieving these objectives, the department has indicated that in evaluating possible alternatives, consideration should be given to various criteria including: effectiveness, targeting, fairness, complexity and fiscal cost. The federal government has indicated, in its current review, that the LCGE will be changed only if there would be clear improvement in tax treatment from the taxpayers' perspective.

The Committee supports the preservation of the LCGE. In fact, it suggests that the benefit could be improved for use as a tool to facilitate the flow of equity into qualifying small businesses, in order to provide an ongoing incentive for future entrepreneurs and outside equity investors to create and grow small businesses. A more detailed development of this topic can be found in the "Financing" chapter of this report under the heading "Equity Financing."

Financing

THE OPPORTUNITY

Today's small businesses are dynamic innovators that will shape the economy of the future. In fact, our economic future is becoming increasingly dependent on the growth of small business enterprises — to create jobs, to diversify economic activity and to compete effectively in the global marketplace. Accessing suitable financial support to provide the opportunity for such growth is critical to the expansion of small businesses. Without adequate financing, the growth of these businesses will be stunted and our future prosperity threatened.

Access to both debt and equity financing is a critical issue for SMEs in Canada. This is especially true for growing small businesses which need different types of financing as they move from initial start-up through early formative development to expansion and long-term viability. There are also stable businesses that do not necessarily pursue growth but still require access to working capital financing to maintain their operations.

The ease with which businesses obtain financing may be influenced by their growth path, their stage of development and their characteristics. Some businesses may find it difficult to access financing if lenders arbitrarily decide to restrict support on the basis of sector, size, experience, business type, region or some other criterion over which the business has no control.

Small business owners seek most of their debt and equity needs from private individuals and financial institutions. The public sector's role has largely been limited to supplementing, and to some extent facilitating, the provision of private sector financing. Though the public sector's role in small business financing is useful, it represents only a small fraction of the overall financing needs of businesses in Canada.

First Principles of SME Financing

- Access to both debt and equity capital is of primary importance for SMEs.
- The level of government debt should be reduced to lower the cost and increase the availability of funds.
- Canadian financial institutions should adopt financing policies and practices that support the development and growth of SMEs.
- Equity financing should be emphasized as a fundamental need of SMEs.
- The supply of patient equity capital should be stimulated through the tax system.
- Not everyone who wants financing should necessarily get it.
- Government intervention in the marketplace should not compete with but should complement private sector initiatives by filling financing gaps not currently served by the private sector.
- Existing government-sponsored small business financing programs should be rationalized.

SME Responsibilities

In order to maximize their ability to access financing, SMEs should:

- **improve management capabilities, especially in areas such as business planning, finance and accounting, and the preparation of cashflow projections;**
- **learn to communicate effectively with investors and lenders and keep them fully informed at all times; and**
- **explore all available sources of debt and equity financing.**

DEBT FINANCING

Small businesses find it difficult to obtain debt financing from traditional financial institutions because the latter claim they are unable to service smaller business loans economically. One of the reasons for this inability is the banks' use of conventional risk assessment policies that compromise the flexibility of their loans officers. This is even more critical given the domination of the chartered banks and the lack of competition in small business lending markets.

Loan Assessment

The small business sector represents a challenge to financial institutions because they incur relatively higher transaction costs in lending to smaller firms. In addition, these institutions believe there are higher risks in small business lending and prefer to reject proposals rather than to charge higher interest or participate in the business, for example, through royalties or equity.

Working Capital

Rapidly growing small businesses, especially in the services sector, are often limited by shortages of working capital. Financial institutions are reluctant to lend them this capital because they lack tangible assets as collateral. Certain regulations prevent certain assets they do have (such as accounts receivable and inventory) from being attached in a preferential manner in the event of a default.

Collateral

Banks have normally required relatively high ratios of collateral coverage for smaller business loans, particularly for working capital. If these ratios change because of declining economic conditions, there is typically a reduction in the line of credit and/or a requirement to pay down the loan with little notice.

Personal Guarantees

Banks claim that personal guarantees are evidence of commitment by business borrowers to their business. They prevent borrowers from taking actions that could weaken the banks' collateral security through the mixing of personal and business assets. As a result, the banks may require the smaller borrower to give a personal guarantee for the full amount of the loan, in addition to business collateral. Such conditions are problematic for most businesses but are particularly onerous for micro-business borrowers who typically have few assets to pledge. Conventional loan assessment practices rarely consider character and a commitment to repay loans.

Lending Gap

All of these factors provide evidence that there is a small business lending gap, particularly for small and micro-businesses that require loans of less than $100 000, that is not being adequately filled by institutional lenders.

Bank Regulations

It has been suggested that regulations and procedures established by the Office of the Superintendent of Financial Institutions (OSFI) to regulate the operations of federally incorporated Canadian financial institutions may restrict the ability and willingness of those institutions to provide financing for small businesses. For example, banks are required by OSFI to adhere to the Bank for International Settlements (BIS) regulations to set aside capital on commercial loans in an amount equal to 8 percent of the value of the loan. It has been suggested that the 8 percent rule may not be appropriately applied to a broadly diversified small business loan portfolio, and that this regulation could have a negative impact on lending to small businesses.[1]

Environmental Liability

Financial institutions are also increasingly reluctant to provide financing on commercial property because of uncertainty about its environmental status. They normally require extensive environmental auditing to determine the value of property as collateral for financing. As a result, environmental legislation and regulations, including provincial initiatives, are imposing large potential costs on small businesses and restricting their access to financing.

Lending to Knowledge-based Businesses

Banks have found it difficult to train their account managers to understand the risks involved in high-growth, knowledge-based businesses and to evaluate their credit applications. They also find it difficult to lend because these businesses tend to have insufficient fixed collateral assets, such as land and buildings, to secure the loans. A higher proportion of their assets take the form of R&D expenditures, human resource skills, or technology-intensive inventory that are difficult to evaluate or have limited value as traditional collateral. In effect, the characteristics of knowledge-based firms make it hard for them to obtain term financing under conventional bank lending guidelines.

Canadian banks do not operate in an unregulated environment. Over the years, they have benefited a great deal from the protection of the Bank Act.... I believe it is time for the banks to give something back. The time has come for the government to exercise leadership and to challenge the banks to sit down and develop concrete ways to help small and medium-sized businesses find the capital they need.[2]

The Honourable Jean Chrétien,
February 11, 1993

INSTITUTIONAL PRACTICES

Chartered Bank Lending

It has been argued that during the recent recessionary period, Canadian financial institutions, particularly the banks, reduced the number of loans they provided to small businesses. The banks have denied that they have a policy of restricting small business lending and have argued instead that the financial situation of many businesses has deteriorated to a point where their businesses no longer warrant consideration for credit. Small businesses, on the other hand, claim that banks are withdrawing credit support from many firms whose performance warrants continuation of financing.

Canadian banks have experienced an increase in business loan losses during the recession, the largest dollar volume of which was from big business. Under those circumstances, prudent financial management dictated that they take remedial action to protect their asset base by becoming more selective in their lending activities. These actions have involved:

- the establishment of a new measurement of profitability under which they attempt to ensure that each individual loan maintains a preset return;

- the development of specific risk assessment criteria, including a low target loan loss ratio for SME loans, that are generally consistent throughout the banking industry; and
- the adoption of a policy of sectoral lending based on criteria according to industry or geography, which could preclude individual loan applications from being considered on their own merit.

All of these approaches to risk reduction inhibit small business lending by the banks.

The chartered banks have traditionally operated widespread branch networks that reach into virtually every community in Canada. In some areas, they are often the only source for financial services and provide virtually all small business financing. Because of efforts to cut costs and because advanced technology is available, the banks have been reducing the number of branches in their networks and consolidating commercial banking operations into a smaller number of large regional centres. This has removed the lending decision-making process from local communities and made it more difficult for small business borrowers to establish effective banking relationships to meet their needs.

Caisses populaires/Credit Unions

Caisses populaires and credit unions make a significant contribution to small business financing in parts of Canada by providing loans at the local community level. In Quebec, the caisse populaire movement is highly concentrated in the Mouvement Desjardins which has 1 323 caisses populaires in that province and 149 in the rest of Canada. They account for almost 25 percent of the commercial loans in Quebec, with $8.2 billion in outstanding loans to small business at the end of 1993, equal to 15 percent of their total assets. In the rest of Canada, the importance of the credit union movement varies, with about 1 000 local credit unions that vary enormously across the country due to differences in provincial regulations and practices. Outside Quebec, the largest credit union movement is in British Columbia where one large institution, VanCity, dominates the credit union market with assets of $3.4 billion. In addition, credit unions represent an important financing alternative in Manitoba, Saskatchewan and Alberta.

Generally, though, credit unions are small independent units that have limited capacity to undertake commercial lending activities, even in provinces that have provided them with these powers. Credit unions are authorized to lend under the Small Business Loans Act (SBLA), and many do lend moderate amounts under this program. There is concern, however, that the federal government has not pursued policies that would promote credit unions. For example, it has not agreed to let them be eligible for direct deposit of government pensions.[3]

Leasing Companies

Leasing companies and other term lenders are active in equipment financing for small businesses with approximately $16 billion in financing outstanding at the end of 1993, the majority with smaller firms. During 1993, leasing firms financed about $6 billion in leases and other term lending instruments. The industry is made up of independent leasing companies, leasing companies associated with manufacturers and the leasing operations of the chartered banks. For many smaller firms, leasing is an attractive form of financing because it can often finance 100 percent of the value of equipment. It does not require the firm to use equity capital for this purpose.[4]

Federal Assistance

The following box summarizes the more prominent of the more than 200 federal government programs created to assist small business. Given the limitations of time and resources, the Committee was unable to perform a comprehensive review of their effectiveness. The information gathered lacked measures of effectiveness that would enable the Committee to evaluate the programs according to business principles. The preliminary review that the Committee did perform, however, suggested that the proliferation of programs has resulted in substantial overlap in program activities and duplication of administrative bureaucracies. All of this increases the cost of delivering government assistance and confirms the need to substantially rationalize government-sponsored small business financing programs.[5]

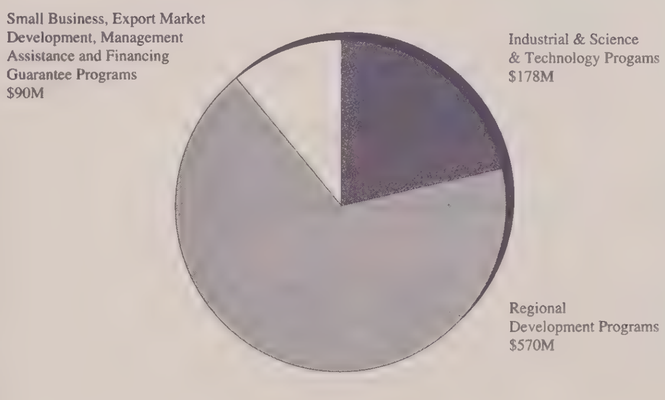
Federal Program Assistance to Small Businesses

The *Small Business Loans Act* (SBLA) provides lenders with a federal government guarantee for losses incurred through small business term loans. The program is delivered by private sector lenders who are the sole decision makers on loan applications. The program provides only fixed-asset-based term loans, with working capital financing being specifically excluded from the program. In 1993, the SBLA was amended to widen eligibility and increase the maximum loan size from $100 000 to $250 000. This has increased the attractiveness of SBLA loans to both borrowers and lenders, and the volume of lending has increased dramatically. However, there is a possibility (dependent upon statistical confirmation) that the increase in the loan size limit under the SBLA has encouraged lenders to service the larger rather than the smaller SME loan market and to shift existing conventional business loans into the SBLA program.

The federal government operates the FEDERAL BUSINESS DEVELOPMENT BANK (FBDB), which has the authority to make commercial loans (including working capital loans) to small businesses that have experienced difficulty in accessing credit from other institutions. Under its existing mandate, the FBDB must operate its financing programs on a full cost recovery basis. However, some observers feel that it is now competing directly with the banks for loans and concentrating on larger small business loans. In 1994, the FBDB's average loan size was approximately $165 000. By dollar value, 11 percent of its loans were for amounts less than $100 0000, 63 percent were less than $500 000, but 39 percent were in excess of $500 000.

The Community Futures Program (CFP) was established to facilitate community economic and employment development, as well as stabilization and adjustment in those non-metropolitan communities that were most in need. Local economic development stimulus is provided through Community Futures Committees (CFCs) that act as strategic planning committees for local communities, as well as Business Development Centres (BDCs) that provide technical and financial support to local small businesses and entrepreneurs to increase and maintain local employment. This program is administered by Human Resources Development Canada (HRDC). A plan is currently being considered to transfer administration of the program to the federal regional development agencies.

Federal Business Assistance Programs
Small and Medium Sized Enterprises
1994-95 Estimates



Source: Department of Finance

To date the major federal regional development agencies, Atlantic Canada Opportunities Agency (ACOA), Western Economic Diversification (WD), Federal Economic Development Initiative for Northern Ontario (Fednor) and the Federal Office of Regional Development – Quebec (FORD-Q) provide project financing for small businesses in designated regions of the country in the form of contributions toward the purchase of equipment, plant modernization and business start-ups, as well as loan guarantees and interest buy-downs. The majority of these contributions are repayable (except for loans under $100 000 in the Atlantic provinces) and targeted to small businesses. These regional agency programs constitute the largest part of federal government program support for small business financing.

Recommendation

The major financial institutions including the chartered banks, caisses populaires, credit unions, and trust and insurance companies must increase their participation in small business financing by establishing more innovative lending programs and techniques and by becoming more active with small business borrowers at the community level.

The federal government must use its leverage to ensure that financial institutions significantly increase their participation in small business lending. The government's regulatory environment should support such lending and encourage increased competition in small business lending markets.

How to Get There

The Committee felt that there are actions required from both financial institutions and the federal government:

Lender Innovations

- develop more cost-effective ways of evaluating SME loan applications
- revise existing risk-rating procedures, including their target loan loss ratios for SME loans, and include more subjective criteria, such as character lending
- expand current small-scale initiatives to find innovative ways of increasing their financing of SMEs by accepting a higher degree of risk through the use of equity kickers, longer-term quasi-equity loans, flexible repayment terms, variable interest payments and royalty-based returns
- accelerate the process of establishing specialized units to service unique small business needs and provide account managers with the skills they will need in the new economy
- negotiate term working capital loans with small businesses based on commitments by borrowers to meet specific financial performance criteria on an ongoing basis
- develop new policies and practices that avoid reductions in lines of credit and/or the requirement to pay down loans with little notice
- support efforts to develop and expand financing techniques for micro-businesses (such as the calmeadow prototype program) that use character and commitment to pay back loans as criteria for borrower collateral.

Improved Lender Services

- improve every aspect of SME customer service
- reduce the turnover of account managers
- provide more relevant training and information to make account managers more sensitive to the unique needs of small businesses in the new economy
- return to community-based commercial banking and extend greater decision-making authority to account managers at the branch level
- introduce, within 90 days, a mediation process similar to the one adopted by the Toronto Dominion Bank that can be used by small business borrowers to settle disputes with the bank regarding the provision or withdrawal of credit. The Committee prefers an effective mediation process capable of dealing with such disputes quickly and cost-effectively to a government ombudsman. The effectiveness and success of this mediation process should be monitored and regularly reported on by OSFI.

Government Action

Consult with representatives of small business to:

- establish new requirements for reporting on small business lending by financial institutions (size and type of loan, characteristics of borrowers)
- have OSFI publish lending data on a quarterly basis
- have lending data reviewed and reported on by the Industry Standing Committee on a regular basis to ensure that the financial institutions are meeting the needs of small business
- encourage the banks to agree to an effective Code of Conduct establishing service standards for small businesses
- impose increased regulation which will compel improved performance if the banks' response to the above is inadequate.

Regulation

- review the BIS capital rules related to SME bank financing and recommend to the other co-signatories to the BIS agreement an approach that would lower the capital requirements for SME loans.

Competition

- increase competition for the chartered banks in small business lending by encouraging the provinces to remove impediments restricting commercial lending that prevent credit unions from competing on an equal footing with other financial institutions, and take steps to promote the use of credit union services
- encourage leasing as an alternate means of small business financing.

Recommendation

The federal government must support small business debt financing by reducing its own debt levels which will serve to lower the cost and increase the availability of funds for small business. This can be achieved by reducing and rationalizing government programs. Remaining government-sponsored programs should be refocused to fill financing gaps that are currently not served adequately by the private sector. Governments must also amend regulations that impact negatively on SME debt financing.

How to Get There

Government Action

- Significantly reduce and rationalize the number and cost of government-sponsored small business financing programs at all levels of government where there is substantial overlap and duplication in both financing activities and administrative bureaucracies.
- Enforce the FBDB's mandate to ensure that its activities are filling the financing gaps confronting small businesses in all regions of the country, including those associated with small and micro-businesses requiring loans of less than $100 000, as well as gaps in regional and sectoral lending and working capital requirements. These objectives should be pursued on a full cost recovery basis.
- Review the recent amendments to the SBLA to ensure that the needs of small and micro-businesses are being met adequately under this program and that financial institutions are not abusing the program by including loans that could be provided under conventional lending criteria.

- Continue to support the Community Futures initiatives, and ensure that the mandate of those successful Business Development Centres (BDCs) remains unchanged and that national coverage is maintained if responsibility for this program is transferred to the federal regional agencies.
- Require that all regional development agencies concentrate on small and micro-business financing and that all loans be repayable with interest at competitive rates though with innovative payment terms.

Regulation

- Work with the provinces to amend environmental legislation so that financial institutions and property owners are not responsible for land-related environmental liabilities that they did not cause. In such cases, property owners should not be restricted in the use of real estate as collateral.

EQUITY FINANCING

Small businesses have problems raising equity capital primarily because of the relatively small amounts of equity that they require versus the costs and risks facing investors in undertaking these investments.[6]

Businesses require equity financing over the growth spectrum, from start-up through development to expansion. Start-up equity financing typically comes from owners or from families and friends, sources that are often soon exhausted and are not normally adequate to allow the owner to finance the development and expansion phases.

Once established and successful, small businesses may meet some of their equity needs from retained earnings. During the early development phase, however, retained earnings are unlikely to be sufficient to finance accelerated growth and small businesses must attract the attention of local informal investors who may bring both capital and expertise to the business. Normally, their capital needs at this stage are less than $500 000.

Very few small businesses are able to generate the high rates of return necessary to obtain financing from venture capitalists during the development and expansion stages. In addition, until their equity requirements are in the $1 million to $5 million range, the high administrative and due diligence costs faced by these investors make it uneconomic for them to provide equity financing in smaller amounts.

Finally, small businesses typically find it difficult to raise capital in amounts of less than $5 million through Initial Public Offerings (IPOs) on the stock markets, or through private placements with long-term investors such as pension funds, life insurance companies and mutual funds, because of the high front-end costs associated with such undertakings. Simply put, venture capitalists and securities offerings do not represent equity financing options for the vast majority of small businesses.

Private Sources of Equity

The primary external sources of equity capital for small businesses are informal investors. They are typically high-income, high net worth business people with a preference for local investments in industries that they understand. They are also willing to invest amounts of less than $500 000 during the development stages and often want to play an active role in management. It is often difficult, however, for investors and small businesses requiring capital to have the same perception of the prospects of the business and to arrive at an investment proposal that is attractive to both parties. In addition, linkages between informal investors and entrepreneurs frequently do not support an adequate exchange of information on investment opportunities and sources of investment funds on the national, regional and local levels.

Both venture capitalists and informal investors often find it difficult to liquidate their investments in small businesses partly because the market for IPOs in Canada has a limited capacity to absorb new junior equity issues. In addition, because of the high costs associated with information disclosure and meeting the requirements of securities regulations, a small business would have to grow to a substantial size before it would be economic to take it public.

Over the years, major financial institutions, including the banks, trust companies, life insurance companies, pension funds and mutual funds, have played a role in providing equity funds through private venture capital companies that operate on a pooled fund basis. Unfortunately, these institutions have recently encountered serious losses in their venture capital activities and have now effectively terminated their provision of equity capital to private venture capitalists. The chartered banks are now investing moderate amounts of capital in specialized expert venture capital funds, but generally, the volume of institutional funds available for equity investment in small businesses has declined sharply.

Knowledge-based Businesses

High-growth and knowledge-based small businesses face more specific difficulties in raising equity capital because of their need to finance rapid growth and their focus on activities, such as R&D, that have a long pay-back period before adequate returns can be achieved on equity capital. In addition, investors require specialized knowledge and expertise to assess the potential of technology-based companies in rapidly growing and changing markets. As a result, most venture capitalists tend to operate through specialized expert funds that pool the capital provided by a group of investors and develop the expertise to undertake equity investments in knowledge-based businesses.

Labour-sponsored Venture Capital

The federal and provincial governments have established tax incentives for the creation of Labour-sponsored Venture Capital Corporations (LSVCCs) that provide equity capital to Canadian small businesses. To date, however, only a limited number of investments have been made in such businesses and some funds are holding much of their assets in short-term money market instruments.

Labour-sponsored Venture Capital Corporations

The federal government provides a 20 percent tax credit of up to $1 000 on the first $5 000 invested in a year, and the governments of Quebec, Ontario, New Brunswick, Nova Scotia and Saskatchewan provide a similar 20 percent credit. Within five years of issuing its first share, a federal LSVCC is required to invest 60 percent of its shareholders' equity in eligible small businesses — less than $50 million in assets and fewer than 500 employees. If there is a shortfall in meeting its 60 percent investment requirement, a portion of the federal tax credit is recovered from the LSVCC along with a penalty of 20 percent of the shortfall. LSVCCs have grown very rapidly in response to these tax incentives and now have approximately $1 billion available for equity investments in small businesses. There is a possibility that these programs have diverted funds that would have flowed to small businesses through other investment channels, had there not been a tax subsidy.[7]

Community Investment Funds

The federal government has committed itself to establishing Community Investment Funds (CIFs) to address the small business need for equity capital. One approach (top-down) would be to provide equity financing for small business by using government funds to leverage the major venture capital investors, such as insurance companies, pension funds, banks and labour-sponsored venture capital

funds. A preferable approach (bottom-up) would be to establish community-based funds that would be aimed at increasing local investment through stimulating the activities of local informal investors. This approach would take advantage of community linkages to encourage investment by these investors, possibly in partnership with institutional sources of capital and/or existing provincial financing programs.[8]

Quebec Community Fund Initiatives

The Caisse de dépôt et placement du Québec has taken the lead in setting up regional pools of venture capital with Desjardins, National Bank and the Solidarity Fund. The Quebec government also plays a role by supplying subsidies to finance investment management activities of regional coordinating committees. Tiny local funds, called Solides, have also been set up to serve the rural local areas of Quebec.

Federal Business Development Bank

The FBDB operates a small venture capital fund that makes equity investments in small businesses in conjunction with its lending operations. The FBDB always remains a minority shareholder and holds investments for an average of four to seven years prior to divestiture. During fiscal 1994, the FBDB authorized equity investments of $9.7 million with a total outstanding and committed of $42.6 million at the end of the year. One result of this activity is that the federal government indirectly becomes an owner of shares in the small businesses in which the FBDB has invested.[9]

Recommendation

The federal government must support the provision of equity financing by providing specific new incentives to encourage the participation of private investors and by ensuring that current incentives are being used effectively. It must also support the establishment of community-based equity financing programs.

How to Get There

New Initiatives

- Adopt tax incentives to encourage individuals to invest in small businesses by reducing the inclusion rate to 50 percent for capital gains on small business investments held for five years or longer and providing a tax free roll-over provision for such capital gains reinvested in small businesses.
- Amend the investment rules for registered retirement savings plans (RRSPs) to permit individuals to invest their RRSP funds in their own (non-arm's-length) private Canadian companies.
- Provide tax incentives, similar to those provided to investors in LSVCCs, to attract private investors to local CIFs and allow capital losses on these investments to be written off against other income.
- Emphasize to the provinces the urgent need to complete the review, harmonization and simplification of securities regulations across the country to reduce the costs associated with new issues of securities, particularly with regard to a simplified prospectus format for small business issues.
- Apply pressure on the major financial institutions, including chartered banks, trust companies, life insurance companies, pension funds and mutual funds, to dedicate some level of their equity investments (including partnering with other investors) to small business investments. The progress in achieving this goal should be monitored and reported publicly on a regular basis.

Current Incentives

- Cap existing tax benefits available to LSVCCs until they achieve their 60 percent investment requirement for small business investments, and amend their investment rules to permit them to invest in expert funds and local and regional small business investment funds such as community-based CIFs. Progress on meeting requirements should be monitored and caps removed only if these requirements are met within set time frames with no extensions provided. A regulatory mechanism should be established to oversee the operations of these funds and ensure that they are meeting their small business investment requirements while following prudent investment practices.
- Require all new LSVCCs to pre-commit to specific quotas for small business investments over a specified time frame.
- Cap the FBDB's venture capital program and privatize it when evidence is available that the gaps being serviced by the FBDB have been filled by the private sector or the CIFs. This would ensure that the FBDB's mandate to fill gaps is being maintained and that the government is not investing in small business shares either directly or indirectly.

Community Programs

- Proceed with the establishment of a locally based CIF program on a pilot-project basis, but without providing any federal government money as investment, either directly or indirectly, in shares of Canadian small businesses. The CIFs should be operated by the private sector in each community, with the government providing a supportive environment by acting as a facilitator. This role could include a subsidy for transaction and/or due diligence costs.
- Encourage the CIFs to share infrastructure facilities and partner with the BDCs and other federal, provincial and municipal financing programs to provide a fully integrated community-based, SME financing program, operating in a cost-effective manner.
- Improve information linkages between informal investors and entrepreneurs at the local, regional and national levels through the establishment of a data base focused directly on these groups, ideally through the Canada Business Service Centres.

It should be added that many of the recommendations concerning small business financing are related to some of the measures proposed in the sections on tax and regulation, both of which have an impact on financing.

The Burden of Government

4

Small business does not believe that governments are serious about reducing paper burden and regulatory problems. They have lost faith. They do not understand and resent governments' continued failure to act on reforms when expectations have been raised.

"Regulatory/Paperburden Issues in the Small Business Sector"

Tourism Canada, 1988

Since the aforementioned report was issued, the situation has deteriorated, not improved.

THE OPPORTUNITY

The burden of government is the intervention and interference of government in the operations of business. It is the effect of regulations that hurt competitiveness. It is the cost involved in complying with regulatory requirements, collecting taxes and responding to information demands from government. And it is the administrative hurdles, the lack of customer service, the delays, the uncertainties and the frustration involved in dealing with public bureaucracy.

The burden of government has a cumulative effect. Every new requirement mandated by governments places yet another weight on the shoulders of business. New demands are continually being added — few are eliminated.

Government burden costs businesses time and money. It costs businesses in terms of competitiveness when regulatory information requirements create inefficiencies, reduce flexibility and impede innovation. This burden is particularly heavy for small businesses who do not have the resources, the personnel, the time or the information to respond to the increasing and varied demands of government.

It is conservatively estimated that regulatory compliance costs the economy approximately $30 billion annually and requires well over 20 000 federal government employees to keep the process lumbering along. The result to business is lost jobs, lost investment, lost opportunities and lost entrepreneurial initiative.[1]

The time to act is now! A concerted effort to reduce the burden of government offers a tremendous opportunity for government and business to realize significant pay-offs: government, because it can no longer afford present levels of intervention in the economy; and business, because the removal of the burden will lead to better productivity, more investment and more jobs. The challenge for governments is to make and keep their commitment to regulatory reform by mustering the political will to act.

SMALL BUSINESS NEEDS:

- TO BE TREATED LIKE A CUSTOMER BY GOVERNMENT — more emphasis is needed on client orientation and service excellence
- SPEED, CLARITY, SIMPLICITY AND FLEXIBILITY — it needs to know what government expects and then it needs the freedom to determine how best to meet those expectations
- TO BE VALUED FOR THE INFORMATION IT PROVIDES — if business is to collect information for governments, it should be allowed to determine how that information is collected; and if a business provides discretionary information, it should be paid
- A SINGLE INFORMATION PIPELINE — the volume in the pipeline must not be too great
- A SYSTEM THAT IS COMPLETELY RE-ENGINEERED AND NOT JUST TINKERED WITH — reductions in the burden of government require new approaches from the ground up, not just pasting solutions over inefficient existing systems
- MORE "BALL PARKING" — as established by the GST Quick Method, which replaced exact accounting-based calculations; this principle should be extended to other taxes and to other forms of regulatory compliance or information collection.

SMALL BUSINESS DOESN'T NEED:

- UNNECESSARY AND COSTLY GOVERNMENT REGULATION
- TO BE TREATED LIKE "SMALL" BIG-BUSINESS — small business structures, financing and human resources differ from those of larger firms
- TO GIVE AWAY INFORMATION FOR FREE — as long as information is treated as a free good, government will not appreciate the cost to business of providing it
- TO ACCEPT ALL CURRENT GOVERNMENT DEMANDS AS MERELY "A COST OF DOING BUSINESS" — the inefficiency of government is hurting Canada's competitive edge
- DISPROPORTIONATE PENALTIES — there is a difference between penalties imposed by governments and those that can be applied to government
- A LACK OF INTERDEPARTMENTAL COORDINATION ON REGULATORY AND INFORMATION REQUIREMENTS
- GOVERNMENT PROGRAMS THAT OPERATE ON A PROCESS, NOT A GOALS-ORIENTED BASIS — often the cost of accessing programs are greater than simply doing it yourself.

The Committee has divided its review of government burden into two main areas: the regulatory burden and the information burden.

REGULATORY BURDEN

The Committee recognizes that regulations are both necessary and can, in some instances, be beneficial to the competitiveness of business, especially when they are designed with the help of businesses affected. However, regulations are rarely established with recognition of the capabilities or the competitive impact on SMEs. Compliance with regulations too often sap SMEs of entrepreneurial initiative and time, both of which are essential to survive let alone compete. Small businesses are disproportionally more vulnerable to the effects of regulations, as they do not have the resources of larger businesses which can more readily absorb or distribute the work load imposed by government demands.

Regulations are usually inflexible instruments that constrain SMEs from introducing innovations that will keep them competitive. Often they are out-dated or incompatible with prevailing market conditions or best business practices.

Small Business Has Some Major Problems with Regulation

- Cost of compliance is too high.
- Unclear requirements — what is expected of small business?
- Uncertainty of interpretation and enforcement.
- Regulations do not recognize the capabilities of, or the competitive impact on, small business.
- Timing of compliance, reporting and monitoring requirements.
- Regulations often reduce flexibility and innovative capabilities.
- Overlap and duplication of government regulations create additional costs to business.
- Regulations are often incompatible with prevailing market conditions, best business-practices, or efficient administration.
- Regulations are often incompatible with the requirements of other domestic or international jurisdictions or of regulating bodies.
- Lack of transparency in regulatory design, interpretation and enforcement.

Many recent regulatory reform initiatives were aimed at increased competitiveness for the entire business community, which is seen by government as a homogeneous entity. Small business is very different — small businesses need flexibility in compliance to ensure equitable treatment under regulatory programs.

Regulatory Flexibility

The principle of regulatory flexibility is based on the recognition that individual businesses, not governments, are in the best position to determine how to meet regulatory objectives in the most effective and efficient manner, taking into consideration the particular circumstances of their businesses.

Current American law requires separate and different treatment for small enterprises. Their *Regulatory Flexibility Act* requires a specific assessment of the impact a proposed regulation would have on small business and provides for mitigating regulations or policies, as appropriate. There is nothing comparable in Canada.[2]

The federal government is considering legislation whereby departments would be permitted to vary the details of regulations, by entering into a compliance agreement with an individual business. This agreement would specify an alternative means for meeting the objectives of the regulations without jeopardizing health and safety.

The process would in theory be available to all. However, the reality would fall short. The ability of SMEs to mount the resources required to prepare the necessary paperwork and negotiate compliance agreements is highly questionable. Special provisions are required to make it simple for SMEs to apply for more flexible application of regulations. This could be achieved through special provisions lessening administrative requirements, or through widespread publication of the terms of compliance agreements reached with the federal government.

Clarity, Accessibility, Interpretation

Regulations are written for governments, by lawyers for lawyers. They are rarely written in clear, plain language understandable to the small-business person. Regulations are usually not accessible. The federal government relies almost exclusively on the obscure *Canada Gazette* to communicate them. Lawyers may read the *Canada Gazette*; small business people do not. In the U.S., this problem was addressed by the *Regulatory Flexibility Act*, which requires departments to find alternative means for communicating with small businesses. Canada needs to follow the U.S. lead in this regard.

The lack of clarity of regulations can produce uneven enforcement or interpretation across Canada. The committee heard examples of businesses that tracked the careers and transfers of enforcement officers who provided good service and fair interpretations, in order to ensure a continuation of clear and consistent enforcement.

Recommendation

The federal government must remove ineffective or uncompetitive regulations that adversely affect SMEs.

The federal government must encourage regulatory flexibility, including systems of self-regulation, in meeting government-defined performance standards. These systems must include specific measures to address small business needs.

The federal government must rationalize existing regulations across departments and jurisdictions.

How to Get There

- Place a moratorium on new regulations until a process is established that can effectively identify and deal with regulatory problems raised by small business.
- Establish a Government Burden Commission, composed of representatives from small business groups and deputy ministers from significant high-burden departments and agencies. Its mandate will be to hold the government accountable to its commitment to reduce government burden. The commission will:
  - review and challenge existing and proposed programs, systems and activities that impose a burden on business, and will exhort the government to undertake significant re-engineering consistent with these recommendations;
  - receive complaints and comments from SMEs and propose means to fix problems; and
  - arbitrate on questions of government burden and report to the appropriate Standing Committee.

The Committee does not want the government to build a bureaucracy around this commission; thus its expenses must be covered from existing budgets.

- Amend the regulatory policy to require regulatory flexibility if a small business impact analysis reveals there would be an undue or disproportionate effect. In such cases, the government should provide a quick method of regulatory compliance including reduced paperwork, monitoring and reporting requirements. Where there is no health and safety concern, a reduced level of compliance including differential standards and reporting requirements, adjusted timetables, or even exemptions from the proposed regulation should be considered in the course of regulatory impact assessments.
- Review and amend, along with the provinces, labour and environmental regulations and legislation to ensure they do not inhibit SME growth and viability.

- Ensure that government training and communications programs include modules on identifying and assessing small business interests (small business representatives should be involved in the development and delivery of these programs).
- Ensure that interpretations of government rules and regulations have an identified shelf-life. Interpretations should be subject to reassessment after no more than five years. At expiration, the government must communicate new interpretations or cease the requirement.
- Allow for compliance agreements with companies (or groups of companies), under which the federal government would agree to eliminate its operating, monitoring and reporting requirements for a business able to demonstrate that it has its own process in place to effectively achieve federal regulatory objectives.
- There must be a quick and simple approval process for compliance agreements with small business. A maximum time frame for approving compliance agreements should be established.
- Ensure that departments accepting compliance agreements develop a communications protocol. SMEs require advance notice of and the gist of compliance agreements, beyond normal gazetting requirements.
- Governments should participate with SMEs in the design of alternative methods of regulation, including self-regulation and the application of economic measures.
- Design enforcement and compliance policies that ensure government regulations will be equally and effectively enforced.

REGULATORY PROCESS

The whole regulatory process, from stakeholder consultations through policy analysis to regulatory drafting and enforcement, must be more sensitive and fair to small business needs. Alternatives to regulations, such as compliance agreements, are being embraced by government without assessing the particular way they affect small business.

Consultations

The federal government's regulatory policy requires consultations with stakeholders before any proposed regulation is submitted to Cabinet. This requirement is too often served in a perfunctory way, after an initiative has already been decided upon. SMEs should be involved from the ground up in designing regulation. Consultations should seek advice from business rather than legitimize decisions already taken.[3]

Impact Assessments

Before a regulation is approved, the drafters must demonstrate to their Minister and Cabinet that certain conditions have been met: the benefits of the regulation must outweigh its costs, and the regulation must "impede as little as possible Canada's competitiveness." The drafters are required to place all this information in a document called a Regulatory Impact Assessment Statement (RIAS). Businesses currently are inclined to view the RIAS as a work of fiction containing puffed-up analyses to justify decisions already taken.[4]

Communications

Regulations are first "pre-published" in the little-read *Canada Gazette*, and after consultations they are published there again. In theory, small businesses wade through this information to find out what is important. In practice, that does not happen. Thus, proposals to regulate and/or the actual regulations are not communicated or understood.

Complaints and Appeals

It is difficult for small businesses to comment on regulations once they have been passed or to complain about the way they are implemented, for example, by a government field inspector. If the owner addresses concerns to the inspector, the inspector will probably respond by saying that he/she has no authority over the way regulations are drawn up or implemented. And if objections are made to treatment received from the inspector, there is no easy avenue for redress.

Review of Regulations

When all is said and done, government's review of regulations are too infrequent, given the fast pace of changing business conditions. Out-of-date requirements often impose costs on business which were unforeseen when the regulation came into effect. There must be a process put in place for periodic assessment and revision of regulations affecting small businesses.

Recommendation

The federal government should publicize and enforce its existing regulatory policy, which states that departments and agencies must justify the need for regulation, weigh the benefits of the regulations against their cost, and determine the relevance, success and cost-effectiveness of existing regulatory programs.

A special provision should be made for assessing the impact that regulations have on small businesses.

Small businesses must be involved in the process of regulatory design, assessment and revision from the very beginning. A process must be put in place for periodic review, updating and revision of regulatory requirements.

How to Get There

- The current federal regulatory policy must be amended by Treasury Board to include the requirement that any measurement of the costs and benefits of a proposed regulation should include a specific analysis of the impact on small businesses by using the Business Impact Test (BIT). This analysis must be part of the RIAS.
- There must be a sunset provision that requires departments to engage in meaningful consultations on their regulations on a rotating basis, beginning every three years and ending within two years.
- A revised Treasury Board consultation and communications protocol should ensure that consultations are an ongoing process, starting with problem identification, continuing through the implementation of the regulation, and using complaints and evaluations as a basis for revisiting the regulation. In effect, complaints are market information. They should be recorded, analyzed and fed back into the regulatory system to correct problems. The government needs to establish some mechanism for feedback to Treasury Board of regulatory assessments conducted by business.
- The government must improve the consultation skills of public servants and ensure they have a better understanding of small business, through developmental training and communications programs.
- Departments must establish protocols for complaint resolution, including a maximum reaction time of 45 days. These should also include an articulated role for regional staff as one focus for the initiation of complaints and for providing feedback. As a general principle, the official through which a complaint originates should be responsible for shepherding it through the system and for reporting back periodically on its status.

- A summary of any proposed regulation should be written in consultation with small business and pre-published in appropriate publications, such as trade magazines, in place of the regulatory policy requirement for pre-publication in the *Canada Gazette*. This summary, like the regulation itself, should be written in plain language.

STANDARDS

Small businesses are increasingly expected to meet a complex and growing array of product, service and operating standards in the private sector. Standards are rules that allow purchasers and suppliers to identify and meet each other's expectations. Standards are the common currency of globalized commerce. Conforming to international standards allows Canadian companies to enter and compete in world markets.

Standards are not only set by governments as part of their regulatory function but also established by Canadian and international standards organizations (with either voluntary or mandatory compliance), by customers and by businesses themselves. They attempt to measure performance, meet operating goals, and improve quality and customer satisfaction.

Standards can have a positive impact on SMEs. They can provide greater security and market certainty to businesses competing with larger companies, both Canadian and foreign, as long as those standards are clearly defined and equally enforced. Standards can assist small business in creating product and service niches and market opportunities, particularly in the field of new technologies. Standards set by customers and met by their suppliers can serve as the basis of long-term relationships between small businesses and their customers, financiers and suppliers. Standards set internally by small businesses can improve quality, efficiency, export readiness and the ability to access financing, and help ensure that regulatory objectives can be met through business practices that are best suited to particular businesses.

Standards can also act as impediments to innovation and growth. They can act as obstacles that keep businesses out of protected markets. They can also be costly to implement. Standards are often set by organizations dominated by the big players in a field. It is the participants around the table that set the standards. Small businesses that are not sufficiently represented stand the risk of becoming standard takers, not standard makers.

Recommendation

The government must encourage SMEs to meet prevailing market standards. Governments must also ensure the interests of small business are not prejudiced in their development, design and application.

The government must act to harmonize standards across departmental and jurisdictional boundaries.

How to Get There

- Recognize, endorse and support the efforts of small businesses to establish and meet internationally designed operating standards. Where company standards meet the regulatory objectives set by government, regulators must not insist on their own less effective and more costly operating procedures. They should instead establish a degree of flexibility by accepting company- or industry-derived operating standards.
- Enhance the certainty of what is expected of businesses and ensure that standards are effectively enforced. Governments should open international and interprovincial markets by reducing non-tariff barriers to trade caused by technical standards and their application.

- Ensure that product, service and operating standards referenced in government regulations are designed with regard to the particular circumstances of small businesses. Governments should ensure that publicly mandated standards minimize cost, maximize competitiveness and certainty in interpretation and enforcement, and reflect prevailing market conditions and customer needs.
- Governments should facilitate the efforts of SMEs to meet product and operating standards by:
  - improving the effectiveness and cost of programs established to help defray the costs of product testing and certification, and ensuring the administrative costs of the program are lower than the cost of do-it-yourself testing and certification;
  - working with small businesses to improve understanding of the benefits of international standards, especially International Standards Organization (ISO) standards; and
  - assisting businesses to participate in ISO standards programs by taking a leadership position (preferably as Chair) in establishing international standards, pushing for international acceptability of Canadian registrars, encouraging joint certification of small business and heightening public awareness of ISO standards.

The committee heard the case of a business that is required by Canadian regulation to submit a bio-tech product, which increases agricultural output, to tests in 11 different ecological zones. U.S. federal government testing requirements see North America as one ecological zone therefore requiring only one test. If you owned that business, what country would you set up shop in?

TESTING, APPROVALS AND CERTIFICATION

Governments spend time, energy and resources protecting themselves in their role as risk managers. A good deal of the certification and testing by governments is to protect both the political and bureaucratic level from public criticism, rather than protecting the public from legitimate health and safety considerations. Government does not know where political risk may arise so it tends to respond by certifying and testing everything. This shot-gun approach to risk management produces delays in the testing, approvals and certification of products.

Time is of the essence for innovative businesses in Canada. If competitiveness is to be enhanced through process and product innovations, bureaucratic red tape cannot stand in its way. The conflict between the dynamism of technology and the lethargy of bureaucracy must be addressed: there is a need to fast-track testing, approvals and certification for Canada's fast-moving businesses.

Time is a particular concern for small businesses that do not have the resources either to push their specific concerns with a slow department or to wait out the long approval time. The long wait for an approval could be a long wait for the only product a small company has to sell. Time is money, and too much time taken may mean the loss of a viable business opportunity and no money for the small firm.

Recommendation

The federal government must speed up testing, approvals and certification processes and ensure that regulatory regimes respond to the needs of Canada's innovative SMEs, particularly in the field of emerging technologies.

How to Get There

- SMEs must be given a fast lane for the approval or certification of new products. To avoid overuse, this fast lane could be available for a limited number of products per year on a pilot basis.

- Negotiate framework agreements with the governments of our major trading partners for international cooperation in the area of testing, standards and certification. These agreements should promote mutual recognition of standards and tests, and sharing the work load for testing new substances.
- Require officials to develop harmonized testing and certification standards, within a very short time frame, and make managers accountable for success in this effort.
- One department, preferably a central agency, must be given a clear and recognized mandate to intervene in cases where regulatory departments are unreasonably delaying the approval or certification of new substances.
- Target advanced technology industries for regulatory review, and streamline testing and certification procedures (e.g. telecommunications, biotechnology, medical devices and pharmaceuticals).

There exists a government policy which states, in part, that "the government [should] ... reduce response burden on the public by eliminating unnecessary collection of information." This policy, called the Management of Government Information Holdings (MGIH) policy, has been largely ignored. Since 1990, the part dealing with paper burden lives in name only.[6]

INFORMATION BURDEN

There is little recognition in government of how its demands for information represent a problem for small business. The complexity, frequency and response time for information requests are still rarely sensitive to the small-business person. Annex A provides a partial list of some of the federal government information requirements imposed upon a retailer/exporter.

Previous Reduction Initiatives

The Committee refers the government to the recommendations of the Nielsen Task Force on Program Review, which produced valuable work that was largely ignored by the previous administration. In 1988, the private sector Advisory Committee on Paper Burden, appointed by the Minister of Small Businesses and Tourism, suggested that a paper burden inventory and an annual paper burden budget would provide the tools for reducing the burden. Those recommendations were never implemented because the public service resisted change while the government lacked the will to override it.[5]

Of the limited government reforms introduced to reduce paper burden, many have relied on technology-based solutions. The problem is not just paper; the problem is burden.

Specific Irritants

Many of the specific information burden irritants cited in this report originated in the departments of Revenue Canada, Statistics Canada and Human Resources Development Canada. The problem, however, exists with most government departments — these departments are most often cited by business owners because they interact with the greatest number of small firms.

Some of the more notable irritants associated with government information burden include:

- different departments asking for the same information — often one department will ask for the same information repeatedly, as in the case of verification of payroll information;
- departments demand information without any apparent sensitivity to the costs it imposes on small business — much of this information is requested because it is free to government;
- information is requested in ways which do not match a firm's records — the time to compile information can be much longer than the time to complete a form (e.g. Record of Employment (ROE), Statistics Canada surveys);

- the ROE must be filled out for any departing employee, regardless of whether or not the form is required for a UI application;
- ROE requires payroll data in a Sunday to Saturday pay week, yet this cycle is used by only one-third of businesses;
- the payroll tax system requires duplicate calculations — CPP/QPP, UI and income tax each require the use of a separate table for employee deductions;
- records retention imposes significant costs — tax, customs and UI records must be maintained for years at the expense of the business;
- simple customs systems do not exist for low-volume importers and exporters;
- information requirements lack clarity, are confusing and unnecessarily complex (e.g. GST, ROE and surveys conducted by Statistics Canada); and
- continuing frustration with GST collection, particularly the lack of harmony in collecting and filing GST as well as provincial sales tax (PST).

THE INFORMATION BURDEN ON SMALL BUSINESS

Small business is the tax collector of government. It collects CPP/QPP, UI and income tax contributions and remits them to government. If it errs, it can be fined. It collects provincial sales taxes, except in Alberta. It collects the GST. SMEs do this work for the government, without payment in most cases, with very little consultation, and with no visible appreciation from government. Small business has earned the right to demand that the system be sensitive to small business and request less time and resources.

Remittances of employee deductions are too frequent. For a small non-automated business, monthly remittances require three times as much paper work and three times as many manual calculations as quarterly payments. Only 15 days are allowed to file most remittances. Small business understands government's wish to receive its money sooner, rather than later. But the cost to small business of those monthly payments is a heavier burden than the inconvenience the government would incur by allowing quarterly remittances.

Procurement and Quick Payment

When small businesses sell products to government, they have to overcome years of practices and government culture that favour large contractors. Government policy, which now has delegated a lot of contracting to individual departments and managers, perpetuates this bias. For instance, small businesses are limited in their ability to compete against large firms through joint ventures with other small firms, because government can hold only one project member liable for all costs.

Most business-to-business contracts require payment for goods and services within 30 days. Not government. Payment is released for mailing 30 days after the invoice is certified. Departments are only required to pay interest after 45 days — in effect enjoying a 15 day "interest holiday." This wait is hard on a small business, because what passes as a small contract for government can represent a sizable part of annual cashflow for a small business. Banks also have very little patience for the cash-flow problems of small business. Government should not be the cause of these problems.

There are a number of other important procurement issues, which are addressed in greater detail in the section on science and technology.

Recommendation

The federal government must immediately assess the scale and scope of the burden problem and target a 10 percent annual reduction of the total information burden over the next five years.

The government must consolidate reporting requirements, define essential information requirements, and impose a moratorium on additional information requirements until such information targets are set.

The government must immediately address specific irritants relating to the information burden on small business.

The government must provide small business with better access to government contracts and provide prompt payment.

How to Get There

- Make a firm policy commitment to reduce the information burden on small business and issue clear guidelines to ensure that this commitment is honoured.
- Mandate Treasury Board Secretariat with overall accountability for reducing of government burden.
- Departments should have their own small business advisory committees. These committees must be able to initiate agendas and topics for discussion.
- Require departments to prepare an "information needs assessment" for any proposed legislation, regulation, policy or program. This assessment must identify any possible information burden. Such information requests can be reviewed by the Government Burden Commission.
- Ensure that information requests are limited to statutory requirements.
- Require departments to develop an inventory of the burdens they impose (Annex B offers specific details to guide implementation). Departments should submit annual information burden reduction plans to Cabinet each year. All the government's information requirements should be reassessed every five years.
- Set up an accountability framework by which managers will be assessed for their success in reducing information burden. A portion of any cost savings should accrue to the responsible managers' budgets.
- Changes to current practices should be demonstrated and evaluated on a pilot basis in a few departments before being extended throughout the government.

Plan of Action to Reduce Specific Irritants

- Review all retention of records requirements and reduce them by at least 50 percent.
- Revenue Canada and Human Resource Development Canada must re-engineer the payroll tax remittance system to reduce the burden on small business. Small businesses require a more sensitive system which consumes less time, is less frequent and recognizes the realities of cashflow.
- Allow small business to provide basic employee and taxation data to one access point from which different departments can obtain their required information. This must lead to simpler filing requirements for ROEs and Statistics Canada surveys.
- Require completion of the ROE only when it is required by the former employee.
- Study the feasibility of extending the ball-parking principle to the collection of taxes and information from micro-businesses (a quick alternative method for income tax).
- Where feasible, small business should be permitted to provide ball-park estimates in lieu of exact calculations for information requests.
- Departments must pay for discretionary information. If information is not required by statute, then departments must be prepared to pay a business to collect, calculate and provide it.
- Any information request must explain the reason for the request, whether or not the request is based in statute, as well as provide a 1-800 number for more information.
- Provide an express system to low-import-volume small businesses so they can use a post-receipt, self-assessment system for customs duties. Exempt these from import controls not related to health or safety concerns.
- The penalties which governments impose and the grounds upon which these are assessed, must be made comparable to the penalties and circumstances under which businesses can charge government (e.g. late payment).
- When the government mandates or requires businesses to perform specific tasks on its behalf, it must cease to punish them for honest mistakes. Specifically:
  - Revenue Canada must reduce the penalties it levies for low instalment payments when these result from unanticipated swings in cashflow.
  - Government should lead by example and pay its bills within 30 days. If late, it must be subject to the same interest and penalty charges that Revenue Canada imposes.
  - Public Works and Government Services Canada should monitor departments' ability to pay on time and hold late paying departments publicly accountable.
- Government purchase orders for goods and services under $10 000 should be accompanied by payment (electronically), post-dated within 30 days.
- Government should encourage joint ventures between small firms by limiting the liability for any one participant to its proportion of the total contract.

Skills Development

5

THE OPPORTUNITY

Small businesses must ensure that the educational skills of both their managers and employees keep up with the changing demands of a volatile, knowledge-intensive and highly competitive economy. When they hire, they want to know that the people they are hiring have the skills they need. And those who want to start new businesses want to know that they can acquire the skills they will need to run it.

> My assets used to be bolted to the floor. Now they walk out the door every night.
>
> *A Canadian entrepreneur on the implications of the new economy*

Both small business owners and their employees need a complex array of skills that will vary by sector and by business. No one is in any position to predict what precise mix of skills will be needed and when. The world is simply changing too quickly. Any attempt to define specifically small business skill requirements could undermine the flexibility that is a competitive advantage of small business. What Canada needs is a highly flexible skills development infrastructure — one that responds to evolving small business needs and adapts to changing conditions. That means a skills development infrastructure that is sensitive to and closely integrated into the dynamics of the workplace and the labour market.

In terms of labour force development, surveys show that 70 percent of all firms provide some form of structured training to their employees and 76 percent provide unstructured training. Among firms employing two to 19 workers, two-thirds provide structured training. Evidence gathered over time suggests that private-sector training efforts are increasing. However, evidence also suggest that many small business managers could benefit from additional training and skills development.[1]

Matching Supply and Demand

As Table 1 shows, there is an extensive network of opportunities for skills enhancement. Small businesses often find it difficult to navigate through what is available to access what will best meet their needs.

Table 1. The Supply Side of Skills Development in Canada

- Community colleges
- University extension programs
- Business schools
- Private trainers
- Business associations
- Apprenticeship
- Co-operative programs (high-schools and university)
- In-house business expertise
- Sector Councils
- Labour Force Development Boards
- Trusted advisers (bankers, lawyers, accountants)
- Business service providers (consultants and intermediaries)
- Federal Business Development Bank (FBDB) Counselling Assistance to Small Enterprises (CASE) programs, Community Business Initiatives
- Human Resources Development Canada (HRDC) programs

On the demand side, there are individuals who want to upgrade their own skills, businesses that want to improve the skills of their existing employees, and managers and business people that would like to hire people with appropriate skills. However, the Committee has observed that if you aim to create wealth, you will create jobs. If you set out to create jobs, you will spend wealth. As long as the government is focused on creating jobs, it may be inclined to adopt approaches that run counter to the logic of the marketplace.

This can be seen in the current focus of HRDC to train unemployed persons for perceived existing jobs or to provide business start-assistance. It is clear that the unemployed need help, and that this should be provided through the UI system. However, if we focus exclusively on artificial training and immediate job creation for the unemployed, other longer-term skill-building and wealth creating opportunities may be lost.

For instance, employed workers should be involved in ongoing skills upgrading, as well as entrepreneurial development. The transition from school to the workplace should be promoted through apprenticeships, co-ops and entrepreneurial education. There is also significant and growing demand for the skills that will be needed to create and fill new opportunities associated with the emergence of the new economy. Training for these jobs of the future will inevitably involve a high degree of entrepreneurial development, in addition to more conventional skills.

The Committee has observed that there is an imperfect match between the supply of and demand for training and skills development in Canada. The best evidence of this is the fact that there are thousands of vacancies for skilled jobs while unemployment rates remain stubbornly high.

Recommendation

All training for small businesses in Canada should move toward a more effective and flexible training infrastructure that responds to small business requirements as they evolve. That means a skills development infrastructure that responds to market signals, training that is shaped by real business needs, and training that is delivered in the most effective location.

Priority Areas for Action

The Committee believes that there are four priority areas in which an opportunity exists for business and governments at all levels to collaborate to improve the Canadian market for skills development:

- rationalize skills development programs offered by governments at all levels as a way of eliminating duplication, cutting costs, improving relevance, and ultimately reducing rigidities and distortions;
- ensure that there is a convenient way in which small businesses across Canada can access all current and pertinent information on training and skills development;
- address the issue of skills development delivery and standards by forming a self-regulating Training-Sector Council for the industry; and
- develop initiatives to help small businesses understand the importance and benefits of enhancing both managerial and employee skills as a way of growing their companies.

RATIONALIZING GOVERNMENT TRAINING

Reform of the government's role in skills development offers a significant opportunity to realize savings, and to apply some of these savings to measures that will improve skills market information.

Human Resources Development Canada

HRDC spends a major part of its budget on social and training assistance for the unemployed. Too much of the training activity supported by HRDC is open-ended, focused on traditional jobs for which demand is weakening and disconnected from the real needs of the marketplace.

In reviewing HRDC's current training efforts, the Committee came to the following general conclusions:

- There is a huge imbalance between efforts directed at social assistance and those directed at developing skills relevant to the job market and to new business creation.
- Current spending on training and skills development is immense. It is not clear that this money is well spent. Program evaluation does not measure effectiveness or impact on the end user in a useful way.
- There is a need to introduce more business-like forms of management and evaluation: programs are not sufficiently accountable in terms of their effectiveness, delivery efficiency and content.
- There is considerable overlap and duplication both within HRDC, and between HRDC and other departments and agencies and other levels of government, in the training programs currently available.

A more balanced policy approach would seek to provide more training and skills development opportunities focused on entrepreneurship, self-employment and business start-ups. Such a rebalancing might better prepare Canadians for taking an active role in creating new businesses and finding new jobs, rather than passively hoping to squeeze into an existing job.

Recommendation

The Committee recommends that Human Resources Development Canada change the balance of its programs away from social assistance and toward market-oriented skills development. It should increase value of taxpayers money spent on programs offered, reduce program proliferation, eliminate overlap and duplication and improve effectiveness, by targeting a 50 percent reduction in the number and cost of programs. These reductions should be undertaken in the interests of improving the focus on those remaining.

HRDC should introduce business-like techniques for program management and evaluation (such as impact on productivity and profitability). It should abandon existing abstract program performance targets. Finally, HRDC should ensure that all training efforts focus on developing skills that are in demand by employers or that can allow people to create their own businesses. In particular, it should place more emphasis on workplace-based training and entrepreneurship development.

Unemployment Insurance

Developmental Uses programs under UI are intended to help unemployed Canadians acquire new skills or upgrade old ones. Not enough of this training, however, is linked to developing the skills that are really needed by small- and medium-sized businesses. At present, UI blurs the distinction between unemployment support and training and it encourages people to make choices on the basis of benefits provided instead of market demand.

After three attempts at reforming UI over the past decade, the system is still in need of an overhaul. The overall UI system remains in debt ($5.9 billion) and costs about $18.5 billion annually.[2] Moreover, UI has evolved to include a variety of social, regional and economic objectives. The system sends the labour market conflicting signals, it includes disincentives to work, it allows for cross-subsidization among sectors, it does not control repeated usage and it is open to abuse.

The recently released proposals for reform of social programs contain suggestions for improving UI. There is an opportunity to tie UI training more directly to business needs, by using it to develop skills that are in demand by employers or can be useful in small business start-up and self-employment.

Recommendation

Training offered under Unemployment Insurance (UI) should be better linked to the real requirements of small business. Training programs should better promote labour market flexibility and mobility, rather than create or reinforce labour market rigidities.

Funds from the UI account should only go to beneficiaries. The account should not be used to fund other labour market and social programs. The Committee and employers are strongly opposed to the creation of any sort of payroll tax for training the general population.

Apprenticeship

A properly functioning system of apprenticeship across Canada could have a positive impact on small business. It could provide potential employers with the assurance that job candidates possess skills conforming to certain standards.

There is evidence of skill shortages in a large number of trades. This reflects the failure of current programs for redirecting and retraining workers to better prepare them for higher-demand occupations. More effective apprenticeship programs could enhance these efforts, especially for unemployed youth.

Many difficulties affecting apprenticeship programs in Canada stem from jurisdictional disputes. They reflect the inability of different levels of government, businesses and unions to work together effectively.

The result of these failings is that of 169 apprenticeable trades in Canada, most are not recognized as such in all 12 provincial and territorial jurisdictions.[3] One goal must be to ensure that all jurisdictions recognize the same set of trades and standards. Another goal should be to expand the number of apprenticeable occupations by identifying others suited to this model of training. There is no reason that the apprenticeship model could not be applied to occupations such as banking, insurance and telecommunications. It should be noted that professions such as medicine and law use a form of apprenticeship (internships, articling) though they do not call it by that name.

Recommendation

The federal government must work closely with provincial and territorial governments, educational authorities, business and labour to extend the apprenticeship model into new trades. It should support efforts to increase the percentage of the labour force that takes advantage of apprenticeship programs, to attract younger people into apprenticeship programs, and to encourage greater harmonization among the provinces and territories in the trades that are recognized as apprenticeable.

How to Get There

The federal government can promote apprenticeship by acting as an honest broker in getting key stakeholders around the table. It can exercise leverage through the funding it provides to apprenticeship programs. While setting out general national objectives and working to secure buy-in from all stakeholders, the federal government should not attempt the kind of micro-management that is more appropriately left to these same stakeholders.

Co-operative Education

Co-op programs offer small businesses an opportunity to hire bright, enthusiastic young people whose skills might be developed and who could become valuable assets for the firms hiring them. Such programs are also a way of developing a pool of labour that has both experience and more relevant skills.

Many young people leave the public education system lacking both practical skills and a realistic idea of what is required in the workplace. By allowing young people direct contact with the workplace, co-operative programs:

- raise awareness of career possibilities and requirements;
- ease the transition from school to work;
- provide participants with experience and marketable skills; and
- provide a future supply of trained labour for business.

According to the Co-operative, Career and Work Education Association of Canada, the number of secondary school students participating in co-op programs has increased more than tenfold since 1984. The number of post-secondary institutions with co-op programs is increasing as is the number of students who participate in them. The proportion of school boards offering secondary co-op in at least one school ranged from 55 percent in Quebec to 100 percent in Prince Edward Island. Within such boards, the proportion of schools offering co-op education ranged from 14 percent to 98 percent and the proportion of students participating was between 1 percent and 11 percent.[4]

Recommendation

Co-operative education is an effective way of giving young people a perspective on skills needed and opportunities available in the workplace. The government should promote and facilitate the expanded use of co-operative programs by all key stakeholders, particularly secondary and post-secondary educational institutions, and small and medium businesses.

ACCESS TO INFORMATION

Business Skills Development Network

Small business would benefit greatly from having more complete and more easily accessible information about skills development opportunities. Such information, for example, can have a significant impact on the ability of small business to secure the skills it needs to access financing. Lenders and investors are keenly interested in the management skills and expertise available to businesses looking for financial support.

The Committee believes that small business would benefit from the creation of a business skills network. Specifically, such a network could provide easier access to:

- materials which can help identify skills development needs and point to solutions;
- comprehensive information about training models and skills development opportunities; and
- reliable and affordable experts and “trusted” advisors who can provide the mentoring and counselling that SMEs might need to assess, plan and implement skills development on an on-demand and customized basis.

The success of such a network will necessarily depend on the private sector which is best equipped to provide training and mentoring. The government should not be involved in delivering training but it can play a useful role by focusing on information dissemination.

In particular, the government can:

- provide information on key aspects of skills development (what is available, from whom and where);

- facilitate the sharing of information about experiences and best practices from one part of the country to another;
- help industries and sectors develop their own national skills and training standards; and
- work with other stakeholders to promote the importance of training and skills development as part of fostering a "training culture" in Canada.

A critical element in making a business skills development network effective is access to information about it. The federal and provincial governments have established Canada Business Service Centres (CBSCs) to provide a "single window" for business-related information from both public and private sources. The CBSCs have the potential of serving as a convenient access point for information on skills development. At present, they are located in major urban centres (at least one in every province), but there are plans to extend access into smaller communities through "satellites" consisting of terminals placed in the offices of business associations or other organizations.

Recommendation

The federal and provincial governments and the private sector must work together to improve the information offered through the CBSCs, particularly by focusing on skills development opportunities at the local level. They must also ensure that CBSC staff are properly trained to ensure quality and consistency of service to small businesses across the country. The federal and provincial governments should partner with non-governmental stakeholders interested in skills development issues to make more information and expertise available and accessible to small businesses.

How to Get There

The CBSC system can provide a useful vehicle for the dissemination of information about the business skills development network. The Committee believes that the CBSCs can do so most effectively if, wherever possible, they build on what already exists. The CBSC information base should be integrated with what is already offered by local business groups, community-based organizations and providers of training. In this way, the information offered through the CBSCs can focus on and reflect what is happening at the local community level and therefore be most relevant and useful to small businesses.

TRAINING STANDARDS

A Training Sector Council

There is no national system of standards for trainers. There is also no national mechanism through which businesses and other stakeholders can provide input on what training standards are needed or how they can be defined.

Such standards would be useful in helping small business differentiate among the many individuals and institutions offering training services. They would provide a set of benchmarks that could be used to guide the delivery of training. They can also ensure that training efforts in Canada correspond to the best available in other countries. Finally, training standards are instrumental in forging the kind of training culture that is key to assuring Canada of its future skill base.

The way that national standards for the training industry can be achieved is to use the Sector Council approach. The development of standards using sector-based councils has been pursued by the federal government from the early 1980s. Sector initiatives have encouraged labour-management collaboration, secured private-sector commitment, supported the development of standards, influenced provincial activities, created new delivery vehicles for skills development, and served to improve harmonization between federal and provincial activities.

Recommendation

Canada's public and private sector educators and trainers should organize themselves into a Training Sector Council. Such a council can be used to market training, administer and regulate itself, as well as to validate training by setting its own standards. The federal government should not get directly involved in articulating labour development or skills standards. It should continue the partnership role it has played with businesses, educators and labour in Training Sector Councils.

How to Get There

A Training Sector Council can be used to forge partnerships between private and public educators. Care will have to be taken to ensure that the interests of private-sector trainers are not overshadowed by the influence of the universities and community colleges.

AWARENESS

Promotion

A key barrier to the improvement of skill levels in Canada is the fact that many people are still not aware of how important skills really are, especially in the new knowledge-based economy that is emerging. Small business owners need to understand and appreciate the extent to which appropriate management and labour skills can enhance their competitiveness and improve their bottom line. In addition, the public at large must recognize the importance of training and accept the reality of lifetime learning as a key to keeping skills relevant.

Such awareness raising is vital in stimulating the emergence of a training culture in Canada. This culture should be focused on entrepreneurship and entrepreneurial development. It is especially important that young people, employees in larger corporations and public-sector workers develop a better understanding of how business works.

The government, working closely with the private sector through business associations, can play a vital role in raising awareness. More specifically, it can help to compile case studies, success stories and examples of best practices that can serve to inspire small businesses and encourage them to adopt similar approaches in their own enterprises.

Recommendation

The private sector and all levels of government must work in partnership to promote a better understanding among small businesses of the important competitive benefits arising from improved managerial and employee skills. Such partnering is key to developing an entrepreneurially oriented training culture in Canada.

Community-based Implementation

Skill building initiatives work best when they are led by the private sector and implemented at the community level. The government's role should be as a catalyst and facilitator: it can help by contributing information, materials and technical assistance, especially as regards best practices in skills development.

Non-governmental organizations (educational institutions, business associations, private trainers, etc.) are already beginning to create local skills development networks. In addition, there are numerous private-sector training initiatives that are taking place at the community level throughout Canada. Moreover, the recently established Canadian Labour Force Development Board and its network of local affiliates are working toward national standards and strategic priorities in the area of training. As this activity increases, it will be important to find out what is going on elsewhere in the country and to share ideas and experiences.

New models of training are emerging. For example, distance education is being used more frequently, especially as telecommunications technologies make this option increasingly cost-effective. Many small businesses might benefit from the application of distance-learning techniques to their own skills requirements, especially in rural areas.

The government should be careful not to compete with private sector providers of training and skills development. In this regard, skills development opportunities offered through the FBDB should complement rather than compete with private-sector offerings. Though the FBDB uses private-sector trainers and counsellors, it subsidizes their services. As a result, end users might find it cheaper to use a trainer through the FBDB than on the open market, even though it may be the same trainer. The net effect could be to distort the operations of the market for skills development.

Since there are already numerous initiatives such as sector councils, labour force development boards, co-op and apprenticeship programs that are having an impact on the skills development marketplace, the government should restrict its role to encouraging such initiatives where there is a significant demand for them.

Recommendation

Skills development initiatives must be focused at the local level. Community-based institutions such as local labour force development boards should be relied on to better match the supply of and demand for workers with particular skills. The federal government must eliminate duplication and competition with private sector training programs.

Science and Technology

THE OPPORTUNITY

The Committee believes that many small businesses could benefit from better access to financing, skilled employees and the application of best practices in management. These factors are particularly important to the success of innovation-based, technology-intensive SMEs. Additional issues such as the protection of intellectual property, early commercialization of research, global competitiveness and familiarity with international marketing are similarly important to these businesses.

In addressing government support in science and technology, the Committee focused primarily on the innovation process as it applied to knowledge-intensive SMEs that tend to perform R&D. Though they are a relatively small percentage of the overall small business population, these firms embody the growth and export potential that is critical to this country's long-term economic success. Moreover, if these firms are successful, their example will inevitably influence many other SMEs across Canada.

There are more than 50 federal programs providing some form of support to science and technology-related activities. Given the number and complexity of these programs and the time available, the Committee did not feel it could comment in detail on each program. In some cases, it was not even possible to get program evaluations that measured efficiency and effectiveness. Instead, the Committee has included a general statement on the hallmarks of a good government program supporting science and technology (see box on the next page).[1]

The Committee's primary thrust is to suggest that the government reallocate existing spending, particularly by focusing on the commercialization of innovation. This should not be understood as an attempt to design new programs or expand the bureaucracy. Instead, the goal is to improve overall effectiveness by focusing on the real needs of innovating small businesses. The Committee's proposals constitute a tangible way of helping growth-ready, knowledge-based firms realize their potential.

The challenge for the federal government is to help create a healthy commercial R&D environment in Canada.

Finally, the Committee chose not to address the broader question of technology diffusion, since this particular issue is being addressed through diffusion mechanisms such as the Industrial Research Assistance Program (IRAP) — the role of which is being reviewed — and the proposed Canadian Technology Network, as well as various provincial and local initiatives.

Innovation and Commercialization

Innovation is the process by which new or improved products and processes are developed and introduced into the marketplace. Technology plays a growing role in the development of new products — as well as in their marketing, production, distribution and after-sales service — but innovation remains an activity where the key assets are people. The process embodies a set of conditions and a series of interactions, relationships or networks among people that help to transform an abstract concept into a marketplace success. Innovation often begins with an idea or a search for a solution or opportunity which is prompted by interactions within firms and among firms, their partners and clients. As a result, clients and partners often create the discipline that guides innovation from concept to commercialization.

Past programs offered at both federal and provincial levels have tended to focus on pushing technology out from laboratories to industrial users. However, in the words of a recent British Columbia review, "any developer's push to get this technology out into the world does not work. Only market

pull has been found effective to draw technology into production." Commercialization and marketing must be recognized from the very beginning as an integral part of the research and innovation process.[2]

Hallmarks of Effective S&T Programs

HOLISTIC: They cover all aspects of the innovation process, from seed assistance for research through development and commercialization. They also recognize the different technological, marketing and management processes that are critical to successful innovation.

NATIONAL COVERAGE DELIVERED LOCALLY: Programs should offer national coverage, but have sufficient flexibility in delivery to adjust for specific local needs.

USER FRIENDLY: Programs should exhibit simple application and assessment requirements, quick turnaround times and be administered by interested and knowledgeable delivery agents.

EMPHASIZE COMMERCIALIZATION: All programs, including the R&D done in government labs and universities, should emphasize marketing and commercialization so that the full potential of an innovation can be realized. Innovation cannot be deemed successful until it is used by society to add value to products and processes.

GENERAL SCOPE BUT DELIVERED BY SECTOR: Programs should be both comprehensive and specific: general enough to apply across a variety of industries, but capable of being tuned to the specific needs of specific sectors. For example, a good program would be flexible enough to meet the specific research, design and marketing needs of designated sectors such as communications, environmental protection or information technology.

ACTIVE MARKETING: Programs should actively focus on real needs and appropriate use. They should make an effort to attract intended users as opposed to the best connected users.

Support for innovation must be closely linked to the marketplace and the commercial potential of the result. Government initiatives should adopt a holistic approach that seeks to help innovative firms succeed in the marketplace. After reviewing a sample of the more than 50 direct assistance programs targeted to science and technology, the Committee found that most tend to focus on basic research, engineering and design. This portion of the innovation process, however, accounts for only a portion of the costs and knowledge required to launch a product.

Innovation and SMEs

While all businesses can benefit from innovation, only a small number of firms have innovation as their raison d'être. According to Statistics Canada, only 0.4 percent of Canadian businesses perform R&D, though more recent evidence suggests that this estimate is low. Governments' Scientific Research and Experimental Development Tax Credit Program assists only a portion of the research done by these companies.[3]

R&D performers tend to be relatively sophisticated, technology-oriented companies with a staff that includes a significant proportion of trained technology specialists. Many of these firms have proven that they can adapt and develop technology, but because of the small size of the Canadian market they are often forced to sell their products internationally before they have significant marketing experience.

Technology-based small businesses are the primary beneficiaries of IRAP. They also tend to use R&D tax credits and high dollar value science and technology-related government contributions and contracts. However, such businesses often need tax incentives, government procurement opportunities and direct assistance to support their initial efforts, build on their core competencies and help them compete in world markets.

TAX INCENTIVES

Tax incentives are seen to be a crucial form of assistance for innovative SMEs because they allow firms to adjust for the costs involved in the inherently risky process of innovation. Canadian sources of financing for knowledge-intensive ventures remain scarce. Many of the SMEs involved in research have relatively few physical assets to pledge as collateral for loans. In such circumstances, the refundable portion (35 percent) of the scientific research and experimental development tax credit and complementary provincial credits allow firms to maintain the cashflow needed to fund innovation projects, especially longer-term efforts.

The *Federal Income Tax Act* provides an "investment tax credit for scientific research and experimental development" at a rate of 35 percent on expenditures up to $2 million and at 20 percent for expenditures beyond $2 million. During 1991, 4 427 claims were made by qualifying CCPC's with credits worth $289 million. Other corporations had 1 822 claims with credits worth $728 million.[4]

The Committee concurred with the findings of *Prosperity through Innovation*, which recommended that the environment for commercializing innovative products and services be improved by relying less on subsidies and grants and more on tax incentives. Specifically, this study recommends that government:

- move away from a narrow interpretation of what constitutes research and development to cover in-house improvement, product development, prototype and pilot plants, and the commercialization of new products, processes and services; and
- examine the eligibility for tax credits of social science research that contributes to the research, development or commercialization of new products processes or services (e.g. ergonomics).[5]

The Committee recognizes that this initiative may not be possible to implement under the current fiscal circumstances, and that it may be difficult to design a program that cannot be abused. However, this approach should be given a high priority. The funding can be found through the elimination of other existing program areas.

Due to a lack of private capital in Canada, more and more small Canadian companies are acquiring financing through the public markets, particularly in the early stages of their growth. The Committee noted that a company listed on some foreign exchanges could maintain its Canadian-controlled private corporation status, while losing this status if listed on a Canadian exchange. These publicly held Canadian-controlled corporations which have recently gone public should not lose their eligibility for the refundable 35 percent Scientific Research & Experimental Development tax credit.

Recommendation

The current federal investment tax credit must be maintained and expanded to include a broader scope of innovation activities.

The government must implement procedures to ensure consistency of interpretation, including a pre-approval and/or summary approval procedure, and simplify audit procedures relative to the Scientific Research & Experimental Development tax credit.

Government must establish an appeal process that is clear, fast and independent, as this is crucial to research performers.

Government should extend eligibility criteria for Scientific Research & Experimental Development tax credits to remain in effect for three years after an initial public offering for Canadian-controlled companies, assuming all other criteria are met.

PROCUREMENT ISSUES

Government S&T procurement policies can have a significant economic impact on all small businesses, and they can play a vital role in stimulating Canadian technology-based SMEs. Procurement can be important in helping SMEs develop new products and become more internationally competitive by providing a vital first sale to the home government, thus adding credibility to the company's international marketing efforts. Many international trade agreements allow governments to use procurement to support SMEs; such activity is recognized and permitted in both the North American Free Trade Agreement (NAFTA) and the General Agreement on Tariffs and Trade (GATT). This is a common practice in the U.S., Japan and Europe.

The Committee believes that the federal government should use procurement on behalf of Canadian SMEs. More specifically, it believes the government should provide technology-based businesses with opportunities to use government S&T contracts to enhance their core competencies and their competitiveness. Procurement contracts are also important in stimulating company expertise in the provision of final goods, services and value-added engineering processes.

There have been some efforts to stimulate government outsourcing of R&D. As of 1972, the private sector has been given access to Canadian government contracts for mission-oriented research, development and feasibility studies in the natural sciences. In 1976, the government extended its program to include: ongoing S&T requirements; scientific activities in the areas of scientific information, testing and standardization; and requirements in the human and social sciences of urban, regional and transportation studies.[6]

Canadian Technology Development Program

Small businesses view securing a government contract as being far more important to their continued growth than securing help from a granting program. Such contracts offer companies the opportunity to provide a solution to government requirements while building on their expertise. A government contract can have a positive impact on a company's cashflow during a crucial stage in the development process, as long as the government is prompt with its payments — an issue touched on in the chapter on "The Burden of Government." Furthermore, winning such contracts is held to be a definitive sign of success. The Committee therefore believes that Canada should implement an initiative similar to the Small Business Innovation Research (SBIR) program in the U.S.[7]

This highly successful U.S. program requires federal agencies to set aside a percentage of their R&D procurement for small businesses, or to ensure that large prime contractors reserve a percentage of their research and development budgets for small business. Agencies are directed to issue an annual SBIR solicitation that sets forth their R&D needs and missions. These are described in sufficient detail so as to assist small firms in providing on-target responses. Since departments must announce their requirements at least three months in advance, this helps smaller companies do forward planning. A

major criterion used in awarding contracts is the commercialization plan attached to the proposal. The program has been extremely successful in stimulating the growth of many innovative small businesses in the U.S. It has earned the respect of venture capitalists who track new SBIR contract winners closely and often invest in them.

Recommendation

Canada should adopt a Small Business Innovation Research Program for Canadian federal research. SME criteria and set-aside percentages should reflect the Canadian situation.

Funding for the program should be redirected from the intramural research budgets of federal agencies.

All intellectual property gained through contracting for government must remain with the Canadian firm, which can then commercialize it.

The granting councils, such as the Natural Sciences and Engineering Research Council, the Medical Research Council, and the Social Sciences and Humanities Research Council, should be directed to reserve portions of their industrial partnerships program matching funds for SME participation.

How to Get There

The Committee's intention is not to create an additional federal bureaucracy, but rather to use existing resources in aid of what is permitted under Canadian trade agreements. For successful introduction, such a program must be backed at least by a Treasury Board Directive, have a simplified application and evaluation process, and early publication of upcoming opportunities to facilitate planning. Participating Canadian businesses will be required to sign an agreement that protects intellectual property developed under this program to ensure that it remains owned by a Canadian corporation for a period of not less than five years.

Procurement of Finished Goods, Services and Engineering Processes

The Committee believes that proof of government procurement is very important in adding credibility to any company's domestic and international marketing efforts. It is especially helpful to small businesses that have developed a product or service they intend to commercialize globally. Government procurement can play an extremely important role in stimulating development of finished goods, services and engineering processes in a wide variety of SMEs. Such initiatives can be implemented in accordance with international agreements and funded from existing program resources.

Recommendation

Government must re-evaluate its in-house purchasing requirements to ascertain the amounts that are currently supplied by SMEs, and mandate an increase in the amounts of these purchases from SMEs by a minimum of 10 percent over the next five years.

Each department should be required to report annually on progress to the Ministers responsible for Public Works and Government Services Canada, Industry Canada and Treasury Board.

Unsolicited Proposals Program

The Unsolicited Proposals Program was created in 1974 to fund new ideas for innovative products and services on a non-competitive basis. Although federal departments were required to sponsor and co-fund proposals with Supply and Services Canada, the proposed product or service could be of long-term interest and not conditional on current needs. The Unsolicited Proposals Program offered bridge

financing for the first year of the project, while the procuring department agreed to provide funding for continued project development for subsequent years.

With an annual budget that reached $23 million in 1989, the program in that year received over 600 proposals and awarded 200 contracts. In 1991, however, the program was reduced to performing a brokerage function. It handled only 114 proposals and granted only 24 contracts for that year. The brokerage program operates without bridge financing and depends solely on funding from sponsor departments on a case-by-case basis. This reduction of the program occurred despite strong support from the private sector and science-based departments.[8]

A recent review concluded that the Unsolicited Proposals Program was a most useful innovation support model. It provided funding to cover prototype development and the "front end" of innovation activity that is problematic for start-ups and small firms. The program funded 100 percent of initial development costs, including an allowance for project overheads.

Recommendation

The Unsolicited Proposals Program should be funded with at least $25 million per annum within five years and given a renewed mandate to assist with bridge financing of innovation projects on a matching basis with the host departments.

Departments should be directed to reallocate a percentage of their capital budgets to unsolicited proposals from small businesses.

How to Get There

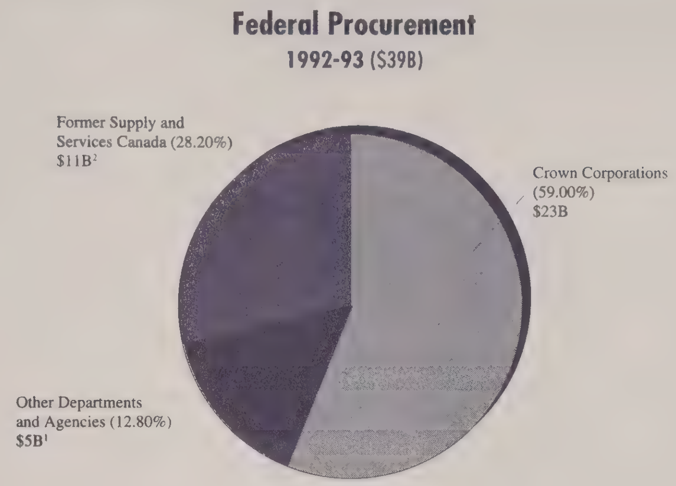
A recent review of the earlier Unsolicited Proposals Program suggested that departmental needs had a major influence on the type of project supported. Interest to the department, rather than commercial potential of the idea, was of paramount concern in many cases. A significant proportion of program funding supported projects consisting mainly of data collection and analysis. This weakness should be addressed in any new program which should:

- focus on the commercial viability of the resulting product;
- be restricted to Canadian SMEs;
- focus on prototype or early-stage commercialization;
- cover no more than 50 percent of development costs from the fund with the remaining 50 percent financed by the client department;
- include a clear evaluation and accounting framework for each project; and
- help SMEs to build and retain their intellectual property.

Privatization/Contracting-Out

Interest in technology transfer has been an ongoing concern in the development of government policy. Useful technology is often developed in government labs or universities, but seldom gets to be commercialized. There is little social and economic benefit from technological innovation unless it can be transferred to firms that can develop and market it. Generally, innovation has a far greater impact if it occurs in the private sector and is focused on commercialization rather than if it is performed by government at taxpayers' expense.

In 1992–93, the Canadian public sector, including all levels of government, spent $106 billion on procurement. The federal share accounts for approximately $39 billion. The Committee feels that many of the services provided by the government to the public are candidates for privatization or commercialization, especially any new or existing services which are technology-based. These services



1. Includes some goods and construction procurement conducted by other departments and agencies.
2. Business volume before departmental amalgamation.

Source: Department of Finance

can be better carried out by SMEs, thus saving the government money, increasing the effectiveness of the service to the public, and providing a stimulus to technology-oriented SMEs. Government should investigate the opportunities and, where feasible to do so, withdraw from offering its services in situations where they compete directly with the private sector.[9]

In addition, the majority of federal S&T work done by departments and agencies is performed internally. A review of fiscal year 1993-94 shows that agencies such as Environment Canada, the National Research Council, Agriculture Canada and Natural Resources Canada all spent over 80 percent of their S&T resources "intramurally."

The Committee also feels that opportunities exist to encourage privatization of some of the research services performed by government laboratories where it is practical to do so and where such an initiative could result in significant savings to the government. It also recommends that simplified procurement procedures be used to outsource some of the services required by government. Special Operating Agencies were not seen as the answer. Contracts for new services arising from technological change should, in the first instance, be offered to the private sector.

A rapid and comprehensive initiative should be undertaken to bring about this commercialization. The process should be overseen by a group with the necessary power to accomplish the task.

Recommendation

The federal government should give consideration to privatizing government services and labs wherever it is feasible to do so. This could be achieved by giving a central agency, such as PCO or Treasury Board specific responsibility for such privatization activity.

DIRECT SUPPORT

Only a few of the more than 50 government programs supporting S&T have proven effective in encouraging SME innovation. The client population served by several of these industrial assistance programs, especially those focused on the defence and aerospace industries, is quite narrow. Many of these programs are seen to be of very little value to small businesses in their present form. What is worse, SMEs end up as "build to print suppliers" with very little opportunity to develop intellectual property. A designated portion of this funding should be refocused so that small businesses can participate in this development work.

The evidence of program evaluations and reviews suggests that the more successful programs tend to involve high knowledge content, localized decision making and flexible delivery applied in a comprehensive manner. IRAP, with its tradition of advisory assistance and access to technical competency, has consistently shown itself to be successful in promoting technology adoption, adaptation and development among SMEs.[10]

Currently, only a handful of programs provide any assistance beyond a strict technology focus. These include marketing and management assistance provided by the regional development agencies, selected Industry Canada sector campaigns (e.g. software), and specialized market assessments provided by the Canadian Industrial Innovation Centre in Waterloo. As an example, the Atlantic Canada

Opportunities Agency (ACOA) and Federal Office of Regional Development – Quebec (FORD-Q) programs demonstrated a comprehensive approach to innovation assistance by offering marketing and management assistance that complemented the help offered by IRAP. This holistic approach to program evaluation is supported by the Committee.

Recommendation

Direct S&T assistance should take a holistic approach to innovation and cover broader technical (e.g. design) and non-technical (e.g. marketing and management) elements of the innovation process.

The Committee endorses the federal government's intention to place the Industrial Research Assistance Program at the core of a Canadian Technology Network intended to help small companies locate, acquire, adopt and manage technologies.

IRAP Technology Advisors should be knowledgeable in all S&T direct assistance initiatives and actively support SMEs to participate in these programs.

IRAP should also be expanded to include industrial marketing advisors and be given additional funding to finance this activity.

A specific portion of existing direct support programs should be reallocated to provide a better focus for small business participation.

Trade Development

7

THE OPPORTUNITY

The global economy has opened up new prospects for those Canadian businesses that are willing to commit themselves to international trade. Some Canadian businesses have already seen the opportunity and Canadian exports are growing. In 1993, for example, they increased by 15.6 percent over the previous year.[1]

A small number of Canadian SMEs have been extraordinarily successful in competing against the best in the world, but they still represent only a fraction of Canada's true potential. Approximately 60 percent of all current Canadian exports are accounted for by 100 companies, yet it has been estimated that about 60 000 Canadian businesses are either doing some direct or indirect exporting or are ready to begin doing so.[2]

Canadian SMEs have only begun to scratch the surface of opportunity. For example, opportunities exist in advanced technologies (telecommunications, biotechnology, advanced materials). These are a natural complement to our traditional competitive advantages. In addition, the emergence of services as a significant and growing component of international trade presents an opportunity for businesses active in everything from engineering to marketing.

Canadian SMEs have both the capacity and the potential to capture a greater share of the value-added embedded in international goods and service trade. Ultimately, exporting is not appropriate for all SMEs. The decision to export, like the decision to grow, is a choice that remains with the businesses themselves.

EXISTING TRADE SUPPORT

The Committee reviewed existing private and public sector initiatives to critique the type and level of support currently available to help SMEs conduct foreign trade. A summary of some of the existing support is outlined in Annex C.

The conclusion to be drawn from a review of the broad range of support available is that there is already a significant amount of private sector, export-related support available to SMEs across a wide range of trade activity. At the same time, the federal government spends some $600 million annually on trade promotion, some of it duplicating services that are already available in the private sector, within the federal government and between different levels of government.[3]

Clearly, there is no need for government to mount new export-related programs and services. More government programs are not the way to encourage small businesses to expand abroad. In fact, the current reliance on government programs to stimulate exporting activity does not seem to have served Canada well — too few SMEs directly export into too few markets.[4]

The Committee believes that it is time for a new approach. Many business people feel that an appropriate role for government is to point small businesses in the direction of private sector providers of export support, rather than attempting to fill that role itself. The primary responsibility for increasing Canada's international trade lies with business, not government.[5]

THE NEEDS CONTINUUM

The Committee identified the following seven basic requirements as an integral part of the ongoing continuum of export-related needs:

- strategic market intelligence
- detailed market research
- financing
- networking — alliances and mentoring
- education and training
- technological support
- promotion.

Each of these needs represents a distinct element that contributes to the overall export process.

The Committee believes that individual businesses are best positioned to determine what they need to enter into and succeed at exporting. They should be free to initiate the process, define it and control it according to their own best understanding of their business interests. The primary role of the government should be to maintain an environment supportive of trade and to ensure that when Canadian businesses compete internationally, they do so on a level playing field.

If Canada's trade efforts are to be effective for SMEs, a first step is to rationalize and reduce government programming at all levels. Where government competes with what is already available in the private sector, it should withdraw. Where there is unnecessary program overlap and duplication, the number of programs should be reduced and their focus sharpened. The Committee believes that these two actions will result in significant savings. It also feels that some of the savings could be reallocated in ways that will provide better incentives and increased export activity.

Getting Export Ready

Successful exporting involves a complex process requiring diligent preparation. That preparation may involve gathering information, acquiring specialized skills, locating appropriate sources of financing, securing access to specialized expertise, finding partners or identifying other key infrastructural elements that can contribute to success. While private sector intermediaries, information providers, business associations and governments are all available to help, ultimately it is up to the SME itself to do its own due diligence and make sure that it is export-ready before it begins to draw on the resources and support that may be available.

AN INCENTIVE: TRADE STARTERS

The Committee believes that a tax incentive would be extremely useful in increasing the number of SMEs exporting successfully to foreign markets. An examination of the needs continuum reveals that a critical step in the export process occurs at the detailed market research stage. This is the moment when a firm moves from expressing a general interest in exporting to making a specific commitment backed by time, effort and money. If SMEs received an incentive at this point, they might be more inclined to make an investment in the development of export markets.

The Committee concluded, therefore, that a refundable tax credit specifically tied to export market development would offer the greatest leverage. Thus, it is recommending a new initiative called Trade Starters.

Trade Starters offers a mechanism to increase the number of Canadian businesses profiting from foreign markets as well as expanding the markets of those already exporting. It also could encourage more Canadian technology to stay at home and use Canada as a base from which to commercialize

Canadian technology into international markets. Trade Starters could also be used to encourage foreign business to establish operations in Canada in order to ultimately serve international markets.

Recommendation

The Committee recommends that the government implement an Export Market Development Tax Credit — a refundable tax credit against foreign market research and development expenditures that have been incurred to support future exports of both goods and services.

How to Get There

The Export Market Development Tax Credit would benefit SMEs and would share some of the characteristics of the Scientific Research and Experimental Development Tax Credit, a highly successful tax incentive. This domestic tax incentive has been extremely well received by business.

Other types of support for small business exporters have also been considered. In the Committee's view however, a mechanism such as a foreign sales corporation tax deduction would not be as effective for small businesses as a refundable tax credit.

The Committee recognizes that in order that such a tax credit contribute to the success of Canadian exporters, it needs to be designed to comply with the GATT and other trade agreements. Research indicates that the proposal can be implemented in a cost-effective manner that conforms to those agreements.[6]

In developing this option, the Committee is aware of the fact that tax credits have been abused in the past. It therefore proposes that additional work be done to determine what safeguards would be required to implement such a tax credit without making it excessively bureaucratic.

Trade Starters will contribute to deficit reduction by reducing/eliminating many of the fixed costs associated with numerous government programs providing subsidies/grants to exporting businesses. Importantly, the proposed Export Market Development tax credit, a variable cost, is payable only against incurred expenses.

A Business Government Partnership in Trade

The primary responsibility for increasing trade lies with business; it is up to business to make itself ready to take up the challenge.

The diversity and complexity of the needs involved in the export process suggest that there is no one simple way of helping SMEs to export. Instead, a variety of solutions are required that depend on a close and ongoing partnership among the key stakeholders involved in the process.

The evidence provided in Annex C suggests that a great deal of support is already available, especially in the private sector; much of the infrastructure is already in place. What is required is better information and better access to information about what is available and how it can be used by the prospective exporter.

Where there are significant gaps in addressing elements of the needs continuum, the private sector, working in partnership with government, can define what is required and play a key role in providing it. There needs to be a strong partnership to coordinate both export-related information and international trade resources to make better use of the existing infrastructure that can support small businesses as they seek to access and take advantage of export opportunities.

Strategic Market Intelligence

SMEs have consistently emphasized their need for accurate information about the opportunities and threats inherent in foreign markets.[7] Most would-be exporters start by assembling basic information. They then quickly move beyond general information and seek to gather the kind of strategic intelligence that is the key to the assessment of and successful penetration of foreign markets. For most SMEs, personal contacts and telephone calls are the best way of getting market intelligence.[8]

> **Once market information becomes part of the public domain, it is no longer market intelligence.**
>
> *Rod White, Small Business Working Committee*

One way in which the federal government has sought to provide companies with strategic market intelligence is through the Trade Commissioners' Service. In fact, the Trade Commissioners' Service is the federal government's single largest trade promotion program. The Service, however, has received mixed reviews from small businesses.[9] Some officers were described as knowledgeable and helpful, while others were not. In some cases, this uneven service reflects the increasing workload and demands made of Trade Commissioners at their posts. Too much time is given over to red tape and report writing rather than getting on with the job of promoting exports. Another major constraint on Trade Commissioners is the number of programs they have to organize for Canadian VIP visitors.

Whatever the reason behind it, inconsistency in the quality of the Trade Commissioners' Service is a cause for concern among small business people. The Committee suggests that the Service could be improved by establishing appropriate customer-oriented service standards and providing sufficient training to guarantee that there is consistency in the services provided as well as sensitivity to the special needs of small businesses.

However, it is clear that the service will be most beneficial to those businesses that are well prepared.

Detailed Market Research

Beyond general strategic intelligence, the next step in the export process is to develop sector-specific, competitive intelligence and detailed market research. Businesses investigating new markets need comprehensive and precise information on market potential, sales leads, distributor contacts, government procurement, partnership opportunities and so on.[10] They also need to develop in-depth knowledge of prospective clients, customers and competitors in their markets.

The type of information provided by existing government-run export promotion services (trade commissioners, desk officers, market reports) is often too general in nature and not sufficiently focused on specific business needs. To satisfy its competitive requirements, every business must perform its own market research, and the considerable time, effort and expense involved constitutes a barrier to export market entry. Hence, the Committee supports the view that a tax incentive at this stage can provide leverage in encouraging SMEs to become profitable exporters.

Export Financing

SMEs often face financing problems when they venture abroad. In many cases, this is because orders tend to be larger than what they are used to and equipped for in the Canadian domestic market.[11] Moreover, payment terms (particularly offshore) tend to be more extended than are commonplace domestically. The reluctance of the Canadian chartered banks to finance foreign receivables has been a serious problem for SME exporters. In addition, there has been a concern about the inability of SMEs to access the Export Development Corporation (EDC) to assist such financing. The following are some significant financing issues facing prospective small business exporters:

- access to equity financing to expand capacity to handle export orders;
- the need for working capital to cover the period from the moment an export order is received and put into production to the date on which it is shipped and billed;
- post-shipment financing, after invoicing, until payment is made (financing of receivables).

In view of the importance of the Canadian chartered banks to the financing needs of Canadian exporters, the Committee encourages the banks to support foreign receivables financing of smaller exporters. To that end, the Committee encourages the federal government, in cooperation with the Chartered banks, to work with Canada's major trading partners to develop reciprocal agreements on the collection of foreign receivables.

The Committee has noted that the Canadian Commercial Corporation (CCC) is currently implementing a Progress Payment Program under which CCC can assist small businesses to arrange for pre-shipment financing. It is important that this program be accessible for foreign sales in general and not be restricted to purchases only to foreign governments or international financial institutions.

Northstar Trade Finance Inc. is a recent innovative export finance company offering term export financing for SMEs. Northstar is owned by the Bank of Montreal, the British Columbia Trade Development Corporation, the Ontario Ministry of Economic Development and the Dalhousie Financial Corporation.[12]

In addition, the Export Development Corporation (EDC) is developing a Master Accounts Receivables Guarantee (MARG) for small businesses under which foreign accounts receivable held as collateral by banks will be guaranteed by EDC, thereby allowing banks to substantially increase their working capital lending to small exporters. The Committee acknowledges the positive intent of all of these initiatives but would specifically encourage EDC and the banks to make the MARG quickly available and accessible at reasonable cost to SME exporters.

Networking — Alliances and Mentoring

SMEs ready to embark on trade-related activities often are in need of the advice and ongoing mentoring that can be provided by experienced trade practitioners, trade associations and experts. Such counsellors can prove an invaluable source of assistance, especially during the early stages of foreign-market penetration. Such experts, advisors and intermediaries are already available throughout Canada. A key challenge for governments and the private sector is to build on current initiatives to ensure export-ready small businesses are matched with the experts and mentors who are best equipped to help them.

Education and Training

There are already several initiatives across Canada that are designed to provide training in trade-related skills. These include courses, diagnostics and business planning tools, as well as seminars and workshops. They are offered by educational institutions, private sector trainers and business associations, as well as federal and provincial government officials. Given the large array of existing training opportunities, a challenge facing small businesses is to learn about what is available and identify those options that are of immediate relevance to their needs.

Technical Support

Information resources can be complemented by the creation of private sector-driven business centres in key foreign markets. Such centres could offer temporary office space and meeting rooms; secretarial support; translation services, access to telephones and faxes; help in arranging meetings; and some market advice. They might be run by a private sector business association which could charge a fee to recover their costs. They would provide Canadian business people with a convenient bridgehead from which to penetrate new and unfamiliar markets. Such centres could better serve small businesses as information exchanges and marketing centres if they are equipped with leading edge technologies, especially access to data bases on trade-related information and computer-based international partnering and data networks such as BCNet.

One concrete opportunity made possible by today's technology is to use video-conferencing and multi-media capabilities to conduct trade fairs at Canadian business centres abroad. These could involve both foreign buyers and Canadians looking for markets abroad. Such facilities would make it possible for small businesses to explore opportunities for exports and foreign partnerships without the risk and expense associated with travelling.

Promotion of Canadian Products and Services

A final need identified by the Committee is to use the positive image of Canada to promote Canadian products, services and capabilities abroad to take advantage of new business opportunities in support of our export-ready small businesses. This should involve creating and promoting a more distinctive Canadian international identity and promoting Canada's reputation abroad by focusing on quality and excellence.

Recommendations

TAXATION

Profit-Insensitive Taxes

The federal government must reduce the burden of profit-insensitive taxes on small businesses, specifically by lowering premiums on Unemployment Insurance and Canada Pension Plan. Such reductions can be realized through restructured programs, improvements in the efficiency of program delivery and reductions in administrative costs.

The federal government must work with provincial governments to ensure that its leadership is followed at the provincial and municipal levels.

Tax Complexity and Compliance

Governments must reduce the complexity and the compliance costs of the tax system through simplification and harmonization. In addition, Revenue Canada's goals in dealing with small business should be efficiency, consistency, cooperation and fairness.

Goods and Services Tax

The federal government must pursue sales tax harmonization. Harmonization must not result in an overall tax increase. Any transition to a new system must not impose increased costs on small businesses.

Corporate Income Tax

The federal government should adopt graduated Small Business Deduction tax rates based on the level of taxable income. At the same time, it should increase the Small Business Deduction threshold to $400 000 to strengthen the equity base of SMEs and to increase growth and job creation in higher-growth SMEs with profits in the $200 000 to $400 000 range.

FINANCING

Institutional Practices

The major financial institutions, including the chartered banks, caisses populaires, credit unions, and trust and insurance companies, must increase their participation in small business financing by establishing more innovative lending programs and techniques and by becoming more active with small business borrowers at the community level.

The federal government must use its leverage to ensure that financial institutions significantly increase their participation in small business lending. The government's regulatory environment should support such lending and encourage increased competition in small business lending markets.

Debt Financing

The federal government must support small business debt financing by reducing its own debt levels which will serve to lower the cost and increase the availability of funds for small business. This can be achieved by reducing and rationalizing government programs. Remaining government-sponsored programs should be refocused to fill financing gaps that are currently not served adequately by the private sector. Governments must also amend regulations that impact negatively on SME debt financing.

Equity Financing

The federal government must support the provision of equity financing by providing specific new incentives to encourage the participation of private investors, and by ensuring that current incentives are being used effectively. It must also support the establishment of community-based equity financing programs.

THE BURDEN OF GOVERNMENT

Regulatory Burden

The federal government must remove ineffective or uncompetitive regulations that adversely affect SMEs.

The federal government must encourage regulatory flexibility, including systems of self-regulation in meeting government-defined performance standards. These systems must include specific measures to address small business needs.

The federal government must rationalize existing regulations across departments and jurisdictions.

Regulatory Process

The federal government should publicize and enforce its existing regulatory policy, which states that departments and agencies must justify the need for regulation, weigh the benefits of the regulations against their cost, and determine the relevance, success and cost-effectiveness of existing regulatory programs.

A special provision should be made for assessing the impact that regulations have on small businesses.

Small businesses must be involved in the process of regulatory design, assessment and revision from the very beginning. A process must be put in place for periodic review, updating and revision of regulatory requirements.

Standards

The government must encourage SMEs to meet prevailing market standards. Governments must also ensure the interests of small business are not prejudiced in their development, design and application.

The government must act to harmonize standards across departmental and jurisdictional boundaries.

Testing, Approvals and Certification

The federal government must speed up the testing, approvals and certification processes and ensure that regulatory regimes respond to the needs of Canada's innovative SMEs, particularly in the field of emerging technologies.

Information Burden

The federal government must immediately assess the scale and scope of the burden problem and target a 10 percent annual reduction of the total information burden over the next five years.

The government must consolidate reporting requirements, define essential information requirements and impose a moratorium on additional information requirements until such information targets are set.

The government must immediately address specific irritants relating to the information burden on small business.

The government must provide small business with better access to government contracts and provide prompt payment.

SKILLS DEVELOPMENT

Flexible Training Infrastructure

All training for small businesses in Canada should move toward a more effective and flexible training infrastructure that responds to small business requirements as they evolve. That means a skills development infrastructure that responds to market signals, training that is shaped by real business needs and training that is delivered in the most effective location.

Rationalizing Government Training

Human Resources Development Canada

The Committee recommends that Human Resources Development Canada (HRDC) change the balance of its programs away from social assistance and toward market-oriented skills development. It should increase value of taxpayers money spent on programs offered, reduce program proliferation, eliminate overlap and duplication and improve effectiveness by targeting a 50 percent reduction in the number and cost of programs. These reductions should be undertaken in the interests of improving the focus on those remaining.

HRDC should introduce business-like techniques for program management and evaluation (such as impact on productivity and profitability). It should abandon existing abstract program performance targets. Finally, HRDC should ensure that all training efforts focus on developing skills that are in demand by employers or that can allow people to create their own businesses. In particular, it should place more emphasis on workplace-based training and entrepreneurship development.

Unemployment Insurance

Training offered under Unemployment Insurance (UI) should be better linked to the real requirements of small business. Training programs should better promote labour market flexibility and mobility, rather than create or reinforce labour market rigidities.

Funds from the UI account should only go to UI beneficiaries. The UI account should not be used to fund other labour market and social programs. The Committee and employers are strongly opposed to the creation of any sort of payroll tax for training the general population.

Apprenticeship

The federal government must work closely with provincial and territorial governments, educational authorities, business and labour to extend the apprenticeship model into new trades. It should support efforts to increase the percentage of the labour force that takes advantage of apprenticeship programs, to attract younger people into apprenticeship programs, and to encourage greater harmonization among the provinces and territories in the trades that are recognized as apprenticeable.

Cooperative Education

Cooperative education is an effective way of giving young people a perspective on skills needed and opportunities available in the workplace. The government should promote and facilitate the expanded use of cooperative education programs by all key stakeholders, particularly secondary and post-secondary educational institutions, and small and medium businesses.

Access to Information

The federal and provincial governments and the private sector must work together to improve the information offered through the Canada Business Service Centres, particularly by focusing on skill development opportunities at the local level. They must also ensure that CBSC staff are properly trained to ensure quality and consistency of service to small businesses across the country. The federal and provincial governments should partner with non-governmental stakeholders interested in skills development issues to make more information and expertise available and accessible to small businesses.

Training Standards

Canada's public and private sector educators and trainers should organize themselves into a Training Sector Council. Such a council can be used to market training, administer and regulate itself, as well as to validate training by setting its own standards. The federal government should not get directly involved in articulating labour development or skills standards. It should continue the partnership role it has played with businesses, educators and labour in Training Sector Councils.

Awareness

Promotion

The private sector and all levels of government must work in partnership to promote a better understanding among small businesses of the important competitive benefits arising from improved managerial and employee skills. Such partnering is key to developing an entrepreneurially oriented training culture in Canada.

Community-based Implementation

Skills development initiatives must be focused at the local level. Community-based institutions such as local labour force development boards should be relied on to better match the supply of and demand for workers with particular skills. The federal government must eliminate duplication and competition with private sector training programs.

SCIENCE AND TECHNOLOGY

Tax Incentives

The current federal investment tax credit must be maintained and expanded to include a broader scope of innovation activities.

The government must implement procedures to ensure consistency of interpretation, including a pre-approval and/or summary approval procedure, and simplify audit procedures relative to the Scientific Research & Experimental Development tax credit.

Government must establish an appeal process that is clear, fast and independent, as this is crucial to research performers.

Government should extend eligibility criteria for Scientific Research & Experimental Development tax credits to remain in effect for three years after an initial public offering for Canadian-controlled companies, assuming all other criteria are met.

Procurement Issues

Canadian Technology Development Program

Canada should adopt a Small Business Innovation Research Program for Canadian federal research. SME size criteria and set aside percentages should reflect the Canadian situation.

Funding for the program should be redirected from the intramural research budgets of federal agencies.

All intellectual property gained through contracting for government must remain with the Canadian firm, which can then commercialize it.

The granting councils, such as the Natural Sciences and Engineering Research Council, the Medical Research Council, and the Social Sciences and Humanities Research Council, should be directed to reserve portions of their industrial partnerships program matching funds for SME participation.

Procurement of Finished Goods, Services and Engineering Processes

Government must re-evaluate its in-house purchasing requirements to ascertain the amounts that are currently supplied by SMEs, and mandate an increase in the amounts of these purchases from SMEs by a minimum of 10 percent over the next five years.

Each department should be required to report annually on progress to the Ministers responsible for Public Works and Government Services Canada, Industry Canada and Treasury Board.

Unsolicited Proposals Program

The Unsolicited Proposals Program should be funded with at least $25 million per year within five years and given a renewed mandate to assist with bridge financing of innovation projects on a matching basis with the host departments.

Departments should be directed to reallocate a percentage of their capital budgets to unsolicited proposals from small businesses.

Privatization/Contracting-Out

The federal government should give consideration to privatizing government services and labs wherever it is feasible to do so. This could be achieved by giving a central agency, such as the Privy Council Office or Treasury Board, specific responsibility for such privatization activity.

Direct Support

Direct S&T assistance should take a holistic approach to innovation and cover broader technical (e.g., design) and non-technical (e.g., marketing and management) elements of the innovation process.

The Committee endorses the federal government's intention to place IRAP at the core of a Canadian Technology Network intended to help small companies locate, acquire, adopt and manage technologies.

IRAP Technology Advisors should be knowledgeable in all S&T direct assistance initiatives and actively support SMEs to participate in these programs.

IRAP should also be expanded to include industrial marketing advisors and be given additional funding to finance this activity.

A specific portion of existing direct support programs should be reallocated to provide a better focus for small business participation.

TRADE DEVELOPMENT

An Incentive: Trade Starters

The Committee recommends that the government implement an Export Market Development Tax Credit — a refundable tax credit against *foreign* market research and development expenditures that have been incurred to support future exports of both goods and services.

Annex A — Typical Reporting Requirements

[The following is a partial list of the information government requires from a typical retailer/exporter.]

Requirement	Frequency
Revenue Canada – Taxation	
• Goods and services tax return for registrants	monthly
• Corporation Remittance Form	monthly
• Summary of Remuneration Paid	annual
• Registered Pension Plan Annual Information Return	annual
• Remittance form for current source deductions	biweekly
• GST customer exemptions	(kept four years for audits)
• Annual corporate tax return (federally incorporated)	annual
Human Resource Development Canada	
• Record of Employment	per transaction (weekly record keeping required, form filled as needed)
Statistics Canada	
• a telephone survey of sales and inventory	monthly
• Survey of employment, payrolls and hours	monthly
• Survey of direct selling in Canada 1993	monthly
• Annual retail trade survey	annual

Annex B — Proposed System for Assessing Information Burden

Activity	Compliance Mechanisms
1. Initial inventory and assessment of paper burden The Management of Government Information Holding policy (MGIH) must require an inventory and assessment of all requests for information which should include the following: a) classes of respondents; b) time required to complete; c) frequency; d) number of information requests; and e) the calculated paper burden (= b x c x d). This inventory has already been completed by Statistics Canada and must be completed by three other departments on a pilot basis within the next 12 months, followed by all other departments in the same time frame.	Departmental inventories and reports of estimated paper burden should be reviewed by Treasury Board (i.e. Cabinet) and forwarded to the House of Commons Public Accounts Committee, as well as the relevant standing committee. A "Government Burden Commission" will be composed of ex officio members from small business groups with deputy ministers from significant departments and central agencies. This commission will review inventories, assessments and annual plans and make their conclusions public.
2. Periodic assessment MGIH requires that all individual information requests must be reassessed every five years, on a rotating basis.	Periodic assessments could be built into departments' standard audit criteria.
3. Annual plans MGIH must encourage departments to achieve net reductions each year. MGIH must direct departments to prepare annual summaries of their information collection activities, including estimated paper burden, yearly additions and deletions, annual targets for paper reduction and the performance against the previous years.	Departments must set up an identifiable and auditable accountability framework, by which managers will be assessed yearly for their success in reducing paper burden. A meaningful portion (i.e. 30 percent) of any cost savings achieved through paper burden reduction should accrue to the responsible managers' budget. Annual paperwork reduction plans should be considered by Cabinet each year, and should be contained in Part III of the *Estimates*, allowing review by the appropriate parliamentary committees. Treasury Board (Cabinet) should set annual paper burden reduction targets for individual departments.

4. Information Needs Assessment MGIH must require that any proposed legislation, regulations, policies or programs, or any individual proposal to seek information from small businesses or to place any other kind of information burden on small businesses, must be accompanied by an Information Needs Assessment, which will identify possible information burdens and justify them on the following basis: • necessary to meet stated government policies and objectives; • is not already available; • maximizes information sharing within and between governments; • estimates and minimizes the burden on small business; • has given special consideration of the burden placed on SMEs and proposed ameliorating conditions.	The Commission will receive copies of Information Needs Assessments and will review them on a sample basis. Departments should have their own small business advisory committees. These committees must be able to initiate agendas and topics for discussion.
5. Transparency MGIH must require that any information request (e.g. a form or survey) will feature: • its rationale; and whether required by law, or discretionary; • a contact and 1-800 phone number for help; • an estimate of the time required to compile the information; • plain language which has been tested in advance through a representative sample of end users.	Any recipient of a form not bearing all of the required information would not be required to complete it.

6. Administration

Treasury Board Secretariat must be solely accountable for the MGIH and for ensuring that regulatory and paper burden issues are addressed in a coordinated manner.

The MGIH policy is not enough. Administration of the MGIH policy must be facilitated with operational guidelines developed by Treasury Board Secretariat to help and guide departments in implementing the policy.

Treasury Board Secretariat must encourage behavioral change by providing departments with information and skills. Treasury Board must ensure that departments design and implement training, communications and monitoring strategies in support of Regulatory and MGIH objectives.

Operational guidelines will include a standardized method for estimating all types of government burden.

Treasury Board's administration of MGIH and the regulatory policy should be evaluated by Cabinet each year, and a description of its related activities should be contained in Part III of the *Estimates*, allowing review by the appropriate Parliamentary committees.

Annex C — Export Support for SMEs

Requirement for Successful International Trade	Support Currently Available
Strategic market intelligence: • opportunities • competition • risks	InfoExport (renamed InfoCentre) DFAIT market reports Private sector market studies (e.g. Economist Intelligence Unit) International agencies (e.g. World Bank and UN country reports) International Trade Centres
Detailed market research • market size • market dynamics • special requirements	Private sector market research firms in Canada and in target country Trade-related publications, journals, sectoral publications, private reports (e.g. bank publications), foreign promotional materials Canadian embassies and Trade Commissioners' Service New Exporters to Border States (NEBS), and similar programs (NEXUS, NEWMEX) Trade missions (organized by DFAIT, business councils, sectoral associations, horizontal associations) Country embassies and trade offices in Canada DFAIT country-specific publications and data bases (e.g. on Mexico) Canadian Business Centres (e.g. in Mexico) FITT course on international market research *CanadExport* newsletter CEA and Export News Bulletin
International business planning	FITT (courses on international entrepreneurship and international management) Private sector trade consultants DFAIT publications (planning tools) Officers in International Trade Centres "In to Win" (Canadian Exporters' Association)

Partnering • choosing appropriate form • identifying prospects • negotiations • contracting	Private sector intermediaries Canadian Trade Commissioners Bilateral Business Councils Trade missions organized by DFAIT, bilateral councils, sectoral associations FITT course on partnering, international trade law “Buddy System” (Canadian Exporters’ Association)
Marketing • positioning • promotion and advertising • selling	Private sector marketing firms, advertising companies Trade shows and exhibitions PEMD FITT course on international marketing InfoExport WINexport database BOSS database Trading houses
Logistics • packaging, labelling, packing • documentation • transport • customs clearance • warehousing • delivery	Export management firms Trading houses Export management firms Freight forwarders Carriers/transport companies Customs brokers Insurance firms EDC (for insurance) Logistics Institute FITT course on international logistics DFAIT publications (e.g. on transportation)
Financing • financial planning • payment instruments • export credits • financing receivables	Private banks (credit instruments, payment mechanisms, credits) FITT course on international financing EDC financial instruments FBDB (export receivables) Canada Commercial Corporation Regional agencies (ACOA, WD, FORD-Q) CIDA (foreign development programs) International agencies (e.g. World Bank credits) Foreign governments

ACRONYMS

ACOA	Atlantic Canada Opportunities Agency
BCNet	Business Cooperation Network
BOSS	Business Opportunities Sourcing System
CCC	Canadian Commercial Corporation
CIDA	Canadian International Development Agency
CISTI	Canadian Industrial, Scientific and Technological Information
DFAIT	Department of Foreign Affairs and International Trade
EDC	Export Development Corporation
FBDB	Federal Business Development Bank
FITT	Forum for International Training
FORD-Q	Federal Office for Regional Development – Quebec
GeoFITT	FITT program for specific geographical regions
IRAP	Industrial Research Assistance Program
ISO	International Standards Organization
ITC	International Trade Centre
NEBS	New Exporters to Border States
NEWMEX	New Exporters to Mexico
NEXOS	New Exporters Overseas
NRC	National Research Council Canada
PEMD	Program for Export Market Development
WD	Western Economic Diversification
WINexport	World Information Network for exporters

End Notes

TAXATION

1. *Growing Small Businesses*, p. 15, 1994 Federal Budget, Department of Finance, Industry Canada.
2. *Globe & Mail*, p. A8, August 16, 1994.
3. *Creating A Healthy Fiscal Climate*, p. 72. Department of Finance, 1994.
4. *Creating A Healthy Fiscal Climate*, p. 71. Department of Finance, 1994.
5. *Creating A Healthy Fiscal Climate*, p. 88, Department of Finance, 1994.
6. *Tax Measures: Supplementary Information*, p. 16, 1994 Federal Budget, Department of Finance.
7. In September 1994, the Department of Finance sent out a letter inviting individuals and association representatives to participate in a consultation exercise on the LCGE. The number of taxpayers in 1991 (26 000) is quoted in Annex B of this letter.

Annex B notes that in 1991, the amount of support for LCGE was $585 million. During a presentation to the Committee, Department of Finance officials stated that their estimates of 1993 LCGE support was $625 million.

FINANCING

1. *Taking Care of Small Business*, p. 32, October 1994.
2. *Speech to the Empire Club*, February 11, 1993.
3. *Taking Care of Small Business*, p. 37, October 1994.
4. *Survey of Industry Activity*, Canadian Finance and Leasing Association, 1993.
5. Federal Program Assistance to Small Business
   - SBLA — Industry Canada/ESBO;
   - FBDB — *FBDB Annual Report*;
   - *Community Futures* — Human Resources Development Canada;
   - *Regional Development Agencies* — Department of Finance;
6. Equity Financing — the following sources were used for this section of the report:
   - *Informal Investors in Canada; The Identification of Salient Characteristics,* Riding et al, May 1993;
   - *The Venture Capital Market in Canada,* Macdonald and Associates, March 1994;
   - *Federal Ontario Liberal Caucus Task Force on Access to Capital by Small Business,* The Mitchell Report, 1994;
   - *Legal and Institutional Barriers to Financing Innovative Enterprise in Canada,* Jeffrey G. MacIntosh, April 1994.

7. Department of Finance, 1994.
8. Industry Canada, 1994.
9. *FBDB Annual Report*, 1994.

THE BURDEN OF GOVERNMENT

1. W.T. Stanbury, *Reforming the Federal Regulatory Process in Canada*, 1971-1992, December 1992, p. 4, in House of Commons Subcommittee on Regulations and Competitiveness, Issue No. 21, citing the Ministerial Task Force on Program Review, 1986.
2. *U.S. Regulatory Flexibility Act: General Account Office Report GGD-94-105*, April 1994.
3. *The Federal Government's Regulatory Policy*, Treasury Board of Canada, Secretariat, Regulatory Policy, October 1992.
4. Treasury Board of Canada (Consulting and Audit Canada), *RIAS Writer's Guide*, November 1992.
5. *Report of the Paperwork Reduction Advisory Committee to the Minister of State (Small Business)*, March 1988.
6. *Treasury Board Manual: Information and Administrative Management*, Chapter 2, Treasury Board of Canada, August 1990.

SKILLS DEVELOPMENT

1. *Upgrading at Work: the Extent and Cost of On-The-Job-Training in Smaller Firms in Canada*, Canadian Federation of Independent Business, February 1992.
2. *Creating a Healthy Fiscal Climate*, p. 71, Department of Finance, 1994.
3. *National Standards for Apprenticeable Trades*, p. 9, Canadian Labour Force Development Board, 1993.
4. *Cooperative, Career and Work Education Association of Canada, Annual Report*, 1993.

SCIENCE AND TECHNOLOGY

1. *Program Review Document — S&T Programs for SMEs,* Young & Wiltshire Management Consultants, 1994.
2. *Moving Forward — The Vision of B.C. Business*, B.C. Chamber of Commerce, May 28, 1994.
3. *Resource Book for Science & Technology Consultations*, Volume 1, p. 11.
4. *Tax Measures Supplementary Information*, 1994 Federal Budget, Department of Finance.
5. *Prosperity through Innovation — Prosperity Initiative*, p. 10, Financing Innovation, 1992.
6. *PWGSC Contracting Document*, Supply Operations Service Branch, April 1994.

7. *Small Business Innovation Research Program*, U.S. Small Business Administration.

8. *Government Procurement as a Social Economic Lever*, Supply Operations Service Branch, Public Works and Government Services Canada.

9. *Selected Science and Technology Statistics 1993*, Industry Canada, 1993.

10. *IRAP Evaluation Study — Final Report,* National Research Council Canada.

TRADE DEVELOPMENT

1. *Canadian Economic Observer*, Statistics Canada, October 1994.

2. *Growing Small Businesses*, p. 38, Federal Budget Document, February 1994.

3. *Steering Committee for the International Business Development Review Report*, p. 2 (Wilson Report), 1994.

4. *Small Medium Sized Enterprises Focus Group Report*, p. 1, E.S. Tunis & Associates (DFAIT), 1994.

5. *Small Medium Sized Enterprises Focus Group Report*, p. 3, E.S. Tunis & Associates (DFAIT), 1994.

6. *Programs to Assist Small Businesses to Enter International Trade*, Williams-MacNeil and Associates, Ottawa, 1994.

7. *Qualitative Research on the International Trade Business Plan*, p. 8, DFAIT, 1994. Almost all DFAIT surveys indicate the primary importance of strategic market intelligence for businesses.

8. *Survey of Canadian Businesses*, p. 5, Task Force on International Market Information and Market Intelligence Network, 1993. *Qualitative Research on the International Trade Business Plan*, p.p. 14-16, DFAIT, 1994.

9. *Small Medium Sized Enterprises Focus Group Report*, pp. 2-4, E.S. Tunis & Associates (DFAIT), 1994. *From a Trading Nation to a Nation of Traders*, p. 38, DFAIT, 1993.

10. *Qualitative Research on the International Trade Business Plan*, p. 8, DFAIT, 1994.

11. *Financing the New Economy*, pp. 18-23, "Export Financing Subcommittee Report," 1994. *Small Medium Sized Enterprises Focus Group Report*, p. 2, E.S. Tunis & Associates (DFAIT), 1994.

12. *Globe & Mail*, *Financial Post*, September 2, 1994.

NOTES

NOTES

NOTES

NOTES